

## **SECURITIES AND EXCHANGE COMMISSION**

### **17 CFR Part 202**

**[Release Nos. 33-8724; 34-54168]**

### **Amendments to the Informal and Other Procedures; Public Company Accounting Oversight Board Budget Approval Process**

**AGENCY: Securities and Exchange Commission.**

**ACTION: Final rule.**

**SUMMARY:** The Securities and Exchange Commission (“SEC” or “Commission”) is amending its Informal and Other Procedures to add a rule that facilitates Commission review and approval of the budget and accounting support fee for the Public Company Accounting Oversight Board (“PCAOB” or “Board”), which is required by the Sarbanes-Oxley Act of 2002.

**DATES:** Effective Date: August 23, 2006.

Transition Dates: The PCAOB must comply with the timetable in § 202.11(c) and utilize a comprehensive strategic plan with respect to its budget and budget and justification no later than its budget submissions for 2008; provided however that the PCAOB and Commission shall use their best efforts to substantially comply with the timetable in § 202.11(c) for the PCAOB budget submission for 2007. This transition provision does not constitute a waiver of the requirement in section 109(b) of the Sarbanes-Oxley Act of 2002 that the PCAOB adopt a budget not less than one month prior to the commencement of its 2007 fiscal year.

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## **SUPPLEMENTARY INFORMATION:**

The Commission is amending its Informal and Other Procedures<sup>1</sup> to add new Rule 11 related to the Commission's review and approval of the PCAOB budget and accounting support fee.

### **I. Background**

The Sarbanes-Oxley Act of 2002 (the "Act") established the PCAOB to oversee the audits of public companies that are subject to the securities laws, in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports. While the PCAOB is a private, nonprofit corporation,<sup>2</sup> it operates under the statutory oversight and enforcement authority of the Commission.<sup>3</sup>

In particular, the funding and budgeting functions of the PCAOB are subject to the express statutory requirement of approval by the Commission. Pursuant to Section 109 of the Act, the Commission is required to approve the PCAOB budget for each fiscal year and the annual accounting support fee that supports the PCAOB's operations.<sup>4</sup>

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<sup>1</sup> 17 CFR 202, et seq.

<sup>2</sup> Sections 101(a) and (b) of the Act; 15 U.S.C. 7211(a) and (b).

<sup>3</sup> The Act vests the Commission with oversight duties and responsibilities, including the duties to appoint the members of the PCAOB, approve PCAOB rules and professional standards for them to take effect, and act as an appellate authority for PCAOB enforcement actions and disputes regarding inspection reports. The Commission also, among other things, may amend existing PCAOB rules, assign additional tasks to the PCAOB as appropriate, oversee the PCAOB's exercise of certain assigned powers and duties, and limit the PCAOB's activities and remove PCAOB members. See sections 101, 104, 105, 107, and 109 of the Act; 15 U.S.C. 7211, 7214, 7215, 7217 and 7219.

<sup>4</sup> Section 109(b) of the Act, 15 U.S.C. 7219(b), which states, in part:

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The Board ... shall ... establish a budget for each fiscal year, which shall be reviewed and approved according to ... [its] internal procedures not less than 1 month prior to the commencement of the fiscal year to which the budget pertains.... The budget shall be subject to approval of the Commission....

Section 109(c)(1) of the Act, 15 U.S.C. 7219(c)(1), which states, in part:

The budget of the Board (reduced by any registration or annual fees received under section 102(e) for the year preceding the year for which the budget is being computed) ... shall be payable from annual accounting support fees, in accordance with subsections (d) .... Accounting support fees and other receipts of the Board ... shall not be considered public monies of the United States.

Section 109(d)(1) of the Act, 15 U.S.C. 7219(d)(1), which states, in part:

The Board shall establish, with the approval of the Commission, a reasonable annual accounting support fee (or a formula for the computation thereof), as may be necessary or appropriate to establish and maintain the Board.

Section 109(d)(2) of the Act, 15 U.S.C. 7219(d)(2), which states, in part:

The rules of the Board ... shall provide for the equitable allocation, assessment, and collection by the Board ... of the fee established ... among issuers, in accordance with subsection (g), allowing for differentiation among classes of issuers, as appropriate.

Section 109(g) of the Act, 15 U.S.C. 7219(g), which states, in part:

Any amount due from issuers (or a particular class of issuers) under this section to fund the budget of the Board ... shall be allocated among and payable by each issuer (or each issuer in a particular class, as applicable) in an amount equal to the total of such amount, multiplied by a fraction –

(1) the numerator of which is the average monthly equity market capitalization of the issuer for the 12-month period immediately preceding the beginning of the fiscal year to which such budget relates; and

(2) the denominator of which is the average monthly equity market capitalization of all such issuers for such 12-month period.

PCAOB Rule 7100, approved by the Commission in Release No. 34-48278 (August 1, 2003), provides a formula for computation of the annual accounting support fee. It states, in part: “The Board shall calculate an accounting support fee each year. The accounting support fee shall equal the budget of the Board, as approved by the Commission, less the sum of all registration fees and annual fees received during the preceding calendar year from public accounting firms, pursuant to section 102(f) of the Act ....”

PCAOB Rule 7101, approved by the Commission in Release No. 34-48278 (August 1, 2003), identifies four classes of issuers and provides for the allocation of the support fee among those issuers.

This statutory allocation of responsibility to the PCAOB, to formulate budgets and accounting support fees in the first instance,<sup>5</sup> and to the Commission, to review and approve them,<sup>6</sup> is designed to assure effective governmental oversight of the budgetary process of the PCAOB. It contemplates a procedure through which (1) an annual determination may be made each year of the appropriate level of PCAOB revenues and expenditures; (2) budget priorities may be established; and (3) information may be furnished in a timely manner to the Commission, and thence to the Congress, the executive branch, and the public, in a manner that will assist the PCAOB in discharging its duties.

The early experience of the PCAOB and the Commission with adoption and approval of annual budgets has revealed the need for a more formal procedure, in particular to establish a clear timetable for each successive step in a more organized budget process. Both the PCAOB and the Commission have expressed a desire to better organize and routinize the annual budget making function. The goal of the new procedures is to improve the timeliness and transparency of the budget process and

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<sup>5</sup> See section 109(b) of the Act, *supra*, and section 101(f) of the Act, 15 U.S.C. 7211(f), which states, in part:

... the Board shall have the power, subject to section 107 – ...

(4) to appoint such employees, accountants, attorneys, and other agents as may be necessary or appropriate, and to determine their qualifications, define their duties, and fix their salaries and other compensation (at a level that is comparable to private sector regulatory, accounting, technical, supervisory, or other staff or management positions)....

See also sections 101(c)(7) of the Act, 15 U.S.C. 7211(c)(7).

<sup>6</sup> To perform this budget oversight and approval function, the Commission, among other things, assesses the PCAOB's funding priorities and competing demands for PCAOB resources. In addition, the Commission considers whether the PCAOB's administrative and financial management are appropriate, whether improved coordinating mechanisms should be developed, and whether unnecessary burdens are placed on the public.

thereby promote high quality decision making. This rule is designed to establish such a process.

## **II. Discussion**

The budget process described below is designed to codify a thorough and deliberative process for both the PCAOB's preparation and the Commission's review of PCAOB budgets. While it is recognized that circumstances might occur that lead the Commission and PCAOB to agree to vary the process from time to time, the Commission expects that it and the PCAOB will follow the practices in the rule to the fullest extent practicable. The Commission also may waive any of the requirements set forth in this rule if circumstances warrant.<sup>7</sup>

References to the "PCAOB" in either this release or the rule are not intended to require a vote or other official action by the members of the Board. Rather, the Commission expects that actions under the rule will be performed as authorized in the Act and the PCAOB's bylaws.<sup>8</sup>

### **A. Timetable**

The rule contains a timetable that is designed to allow for a more meaningful dialogue between the PCAOB and the Commission regarding the content of each budget. The events and dates set forth in the timetable refer to the year immediately preceding the budget year.<sup>9</sup>

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<sup>7</sup> In addition, the Commission and PCAOB may assess whether changes to the rule are appropriate after the completion of one or more budget cycles.

<sup>8</sup> The PCAOB's bylaws are available on the PCAOB web site: <http://www.pcaobus.org/>.

<sup>9</sup> The PCAOB has a calendar-year fiscal year. If the PCAOB changes its fiscal year to end on a date other than December 31, the Commission would interpret the timetable so that the dates would be adjusted accordingly. For example, the narrative discussion of the PCAOB's program issues and

The first item in the timetable calls for the PCAOB, by March 15<sup>th</sup>, to provide the Commission with a narrative description of its program issues and outlook for the budget year. This narrative is to contain a discussion of the significant factors that the PCAOB anticipates may impact its resource needs in the budget year. The second step is for the Commission, after consideration of the PCAOB narrative, to provide the PCAOB with budgetary guidance and economic assumptions by April 30<sup>th</sup>. The nature and extent of guidance and assumptions may vary from year to year and may include general information about the securities markets, the accounting profession, and other factors impacting the range of budget resources that, in the opinion of the Commission, are needed by the PCAOB to carry out its statutory responsibilities.

The timetable calls for the PCAOB to provide the Commission each fiscal year with a preliminary budget for the next fiscal year, and with a justification for that preliminary budget, on or before the end of July. The new rule states that the budget and budget justification should include, among other things, a detailed budget plan, analyses of the PCAOB's programs and what the PCAOB expects to accomplish in the coming budget year, and a discussion of how the performance of the programs detailed in the budget will lead to both the accomplishment of the PCAOB's long-term strategic goals and the fulfillment of the PCAOB's duties and responsibilities under the Act.

The timetable allows three months following the submission of the preliminary budget and budget justification, August through October, for the Commission to analyze the PCAOB's background materials and the documentation for its budget, and for the Commission and the PCAOB to discuss the PCAOB's programs, assumptions, projected

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outlook for a fiscal year would be due on or before the fifteenth day of the third month of the preceding PCAOB fiscal year.

expenditures and receipts, and other information in or relevant to the preliminary budget and the budget justification. By the end of this three month period, the timetable calls for the Commission to “passback” the budget to the PCAOB with suggested revisions and the Commission’s preliminary views on the budget.

As required by section 109 of the Act, the timetable provides for the PCAOB to approve its final budget before the end of the next month, which would be November 30. As a result of the thorough process preceding the PCAOB’s approval, the PCAOB should be in a position to submit its final budget to the Commission immediately after the PCAOB approves it. This should permit the Commission, which would be familiar with the budget based on the review of the preliminary budget and the budget justification and communications with the PCAOB, to vote whether to approve the PCAOB budget and the accounting support fee on or before December 23<sup>rd</sup> of each year.

In the course of reviewing prior PCAOB budgets, SEC Commissioners and staff have met with PCAOB Board members and staff to discuss matters related to the budget and the Commission understands that PCAOB Board members and staff will continue to make themselves available for such meetings. In addition, to the extent determined appropriate, the Commission may ask the PCAOB to participate in meetings of the Commission to discuss matters related to the budget and the PCAOB has expressed its willingness, if requested by the Commission, to participate in such meetings.

#### **B. Contents of the Budget and Budget Justification**

As noted above, the rule provides for the preliminary budget, the budget submitted for Commission approval, and the accompanying budget justifications to include comprehensive explanations of the PCAOB’s budget plan, past and projected

performance, and strategic goals. Under the rule, the budget justification includes a “performance budget” for the budget year, which, among other things, details what the PCAOB plans to accomplish, organized by strategic goal, and a description of the resources, means and strategies needed to accomplish those targets. The performance budget also would contain the performance targets for the current year and the previous year<sup>10</sup> and describe the resources, means and strategies needed to accomplish those targets.

To facilitate analyses of the PCAOB’s progress in meeting its goals and any trends in its performance and financial operations, the rule provides for each budget to include, among other information, projected, and to the extent available actual, expenditures and receipts for the budget year, the current year and the previous year (for a total of three years).<sup>11</sup> The new rule also states that the budget will include beginning-of-year and end-of-year headcounts for each program area. In addition, to facilitate the Commission’s analysis and approval of the budget, the rule indicates that the Commission expects the budget and budget justification either to be consistent with or to explain any deviations from the guidance and economic assumptions previously provided by the Commission.

The new rule allows the PCAOB to include in its budget and accounting support fee amounts that are necessary to build a reserve not to exceed the obligations expected to

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<sup>10</sup> For example, if the budget year is 2009, the current year (in which the 2009 budget is being prepared) would be 2008, and the previous year would be 2007. The Commission also recognizes that, until the PCAOB publishes a comprehensive strategic plan, an increased number of performance targets may be described in more qualitative than quantitative terms.

<sup>11</sup> Projected and actual expenditures include salary, benefits, relocation and similar benefits. The Commission will review such expenses to assess whether they are consistent with statutory criteria.

be incurred during the first five months immediately following the budget year, in order to provide that the delays in the billing and collection of the accounting support fee that are inherent in the statute, and significant unforeseen events, should not threaten the liquidity of the organization. The funds in that reserve, however, may be used only in accordance with the budget for that following fiscal year or a supplemental budget, as approved by the Commission.

If the Commission has not approved a budget for a PCAOB fiscal year before the beginning of that fiscal year, the rule provides that the PCAOB may spend funds from its reserve and continue to incur obligations as if the last PCAOB budget approved by the Commission were continuing in effect for the new fiscal year.

### **C. Commission-Approved Budgets**

The statutory requirement that the Commission approve the PCAOB budget, contained in section 109 of the Act, is consistent with the general oversight responsibility with which the Commission is charged in section 107. These responsibilities for the budget and operations of the PCAOB require the ability to promote changes in the PCAOB budget when the Commission believes those changes are necessary or appropriate. The rule makes clear, therefore, that while the Commission may not directly change the budget, it may make its approval of a budget conditional on changes to amounts and other aspects of the budget. The PCAOB, in turn, will have the opportunity to consider the proposed changes and to vote again for final approval with or without the changes. To prevent the possibility of missed deadlines, if differences have not been resolved by December 23 then the terms of the most recent conditional approval would become the final budget.

The budget approval requirement is also made more meaningful by limiting the PCAOB's ability to incur expenses and obligations to the general terms of the Commission-approved budget. The rule makes clear that the PCAOB may not spend in a budget year more than the overall expenditure amount specified in the Commission-approved budget and may not transfer more than \$1,000,000 into or out of any program area without prior Commission approval of a supplemental budget. The rule also makes clear that, once a budget is approved by the Commission, the PCAOB cannot use its resources in a manner that is not fairly implied from the approved budget. For example, without Commission approval, the PCAOB may not create a new program to perform functions that are not included in that budget, or eliminate a program that is described in that budget.

#### **D. Supplemental Budgets**

The new rule provides procedures for the PCAOB to seek Commission approval either to spend amounts in excess of, or contrary to, the spending limitations set forth in the rule. In these cases, the new rule provides for the PCAOB to submit a supplemental budget to the Commission.<sup>12</sup> The supplemental budget is to describe, among other things, the events or circumstances necessitating the supplemental budget request, why the request should not or can not be postponed until the next regular annual budget process, and the proposed source for the funds, including any offsets to be made in other programs and activities.

#### **E. Records**

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<sup>12</sup> If there is an urgent need for the PCAOB to obtain approval of a supplemental budget, the Commission may act by duty officer or other means to expedite the approval process.

Under section 107(a) of the Act,<sup>13</sup> the Commission may adopt rules requiring the PCAOB to make, keep, and furnish to the Commission such records and reports as the Commission prescribes as necessary or appropriate in the public interest.<sup>14</sup> In addition, all records of the PCAOB are subject to reasonable examinations by the representatives of the Commission as the Commission deems necessary or appropriate in the public interest, or the protection of investors, or otherwise in furtherance of the purposes of the Act.<sup>15</sup> Pursuant to this authority, as well as the authority inherent in its duty to approve the PCAOB budget, the new rule requires that the PCAOB maintain, and make available to the Commission upon request, a strategic plan and other records in reasonable detail that support each budget and budget justification.

In addition, the rule requires that the PCAOB prepare a report of its spending and staffing levels for each quarter, comparing those levels to the levels in the Commission approved budget. Within 30 business days after the end of the quarter, the PCAOB is required to provide a copy of that report to the Commission.

#### **F. Publication of Budget**

Under the new rule, the interchange between the Commission and the PCAOB on budget matters would begin with the PCAOB providing a narrative description of its program issues and outlook in March and conclude with the Commission vote in December. After the PCAOB provides the Commission with a description of program issues and outlook, the Commission and PCAOB together will discuss ideas and consider

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<sup>13</sup> 15 U.S.C. 7217(a), which provides that sections 17(a)(1) and 17(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”), 15 U.S.C. 78q(a)(1) and 78q(b)(1), shall apply to the PCAOB as fully as if the PCAOB were a “registered securities association.”

<sup>14</sup> Section 17(a)(1) of the Exchange Act, 15 U.S.C. 78q(a)(1).

<sup>15</sup> Section 17(b)(1) of the Exchange Act, 15 U.S.C. 78q(b)(1).

initial recommendations and proposals before the PCAOB approves its final budget in November. During these initial discussions, neither organization will publish the PCAOB's budget, budget justification, supplemental budget, or any underlying materials not otherwise intended for public distribution, until the time the budget is approved by the PCAOB and submitted to the Commission for approval.<sup>16</sup> Once the PCAOB submits its budget to the Commission, the rule provides for public disclosure, subject to any applicable exemption under the Freedom of Information Act,<sup>17</sup> of the PCAOB budget and budget justification, including the PCAOB's "performance budget" for the budget year.

### **G. Definitions**

The rule defines certain terms that may arise in the discussion of budget matters. The definitions are generally consistent with Office of Management and Budget guidelines but have been adapted to apply to a private organization with the character and functions of the PCAOB.<sup>18</sup>

## **III. Administrative Procedure Act, Regulatory Flexibility Act, and Paperwork**

### **Reduction Act**

The Commission finds, in accordance with Section 533(b)(3)(A) of the Administrative Procedure Act ("APA"),<sup>19</sup> that this revision relates solely to agency

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<sup>16</sup> This limitation does not restrict individual PCAOB members from generally commenting on their individual views of the funding requirements of the organization or the status of the Board's deliberations, either before or after the PCAOB adopts its budget.

<sup>17</sup> Certain exemptions under the Freedom of Information Act ("FOIA"), including the exemption for confidential financial information, may apply to some of the information provided to the Commission.

<sup>18</sup> See generally, Office of Management and Budget Circular No. A-11, at ¶20.3 (June 2005).

<sup>19</sup> 5 U.S.C. 553(b)(3)(A).

organization, procedure or practice. It is, therefore, not subject to the provisions of the APA requiring notice and opportunity for public comment. The Regulatory Flexibility Act,<sup>20</sup> therefore, does not apply. Similarly, because these rules relate to “agency organization, procedure or practice that does not substantially affect the rights or obligations of non-agency parties,” the Commission is not soliciting comments for purposes of the Small Business Regulatory Enforcement Fairness Act.<sup>21</sup> The rules do not contain any collection of information requirements as defined by the Paperwork Reduction Act of 1995, as amended.<sup>22</sup>

#### **IV. Costs and Benefits of the Amendments**

Taken as a whole, the Commission’s rules of practice, such as Informal and Other Procedures, create governmental review and remedial processes. That is, they are procedural and administrative in nature. The benefits are the familiar benefits of due process: notice, opportunity to be heard, efficiency, and fairness. These benefits are particularly applicable to the current amendments because the timetable, procedural steps, and materials that are to be made available for Commission review should provide for a more meaningful dialogue between the Commission and the PCAOB and enhance the efficiency and fairness of the budget approval process. In addition, the PCAOB should benefit by beginning each fiscal year with an approved budget, rather than operating for the first few months of the year without such a budget.

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<sup>20</sup> 5 U.S.C. 601 et seq.

<sup>21</sup> 5 U.S.C. 804(3)(C).

<sup>22</sup> 44 U.S.C. 3501 et seq.

In general, the costs of the procedures in the Commission's rules of practice, including Informal and other Procedures, fall largely on the Commission. In this instance, the Act already requires the PCAOB each year to prepare and submit a budget to the Commission for approval. While we anticipate that in the coming years the PCAOB will devote more resources to the preparation of its budget, many of the cost increases in this area are inherent in the maturing nature of the organization and are not attributed solely to the adoption of the amendments. The implementation of a more detailed budget process and the preparation of the materials that would be submitted under the amendments, including quarterly updates on spending and staffing levels, are fundamental to the effective management of a mature organization. Further, conducting the budget preparation process over the period set forth in the new rule should make it a more efficient and effective process.

As noted, the amendments set forth in this release relate to internal agency management, increase the efficiency of the Commission's approval process, and promote timely and meaningful communications between the Commission and the PCAOB.

## **V. Effect on Efficiency, Competition and Capital Formation**

Section 2(b) of the Securities Act of 1933<sup>23</sup> and Section 3(f) of the Exchange Act<sup>24</sup> require us, when engaging in rulemaking that requires us to consider or determine whether an act is necessary or appropriate in the public interest, to consider whether the action will promote efficiency, competition, and capital formation. Section 23(a)(2) of

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<sup>23</sup> 15 U.S.C. 77b(b).

<sup>24</sup> 15 U.S.C. 78c(f).

the Exchange Act<sup>25</sup> prohibits us from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

The amendments are intended to facilitate the Commission's process for approving the PCAOB budget. The amendments increase the efficiency of the Commission's approval process. The rule applies only to the PCAOB, which is an organization established by Congress in the Act, and therefore the Commission does not expect the rule to have an anti-competitive effect. Since there will be an increase in efficiency, there will not be any adverse impacts on capital formation.

## **VI. Statutory Basis and Text of Amendments**

These amendments to the Informal and Other Procedures are being adopted pursuant to statutory authority granted to the Commission, including Section 19(a) of the Securities Act of 1933, Sections 17 and 23(a) of the Securities Exchange Act of 1934 and Sections 3(a) and 101 through 109 of the Sarbanes-Oxley Act of 2002.

### **List of Subjects**

#### **17 CFR Part 202**

Administrative practice and procedure, Securities.

### **Text of the Amendment**

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

#### **PART 202 – INFORMAL AND OTHER PROCEDURES**

1. The general authority citation for part 202 is revised to read as follows:

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<sup>25</sup> 15 U.S.C. 78w(a)(2).

**Authority:** 15 U.S.C. 77s, 77t, 78d-1, 78u, 78w, 78ll(d), 79r, 79t, 77sss, 77uuu, 80a-37, 80a-41, 80b-9, 80b-11, 7202 and 7211 et seq., unless otherwise noted.

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2. Add §202.11 to read as follows:

**§ 202.11 Public Company Accounting Oversight Board budget approval process.**

(a) Purpose. These procedures are established in connection with consideration and approval of the budget and the accounting support fee for the Public Company Accounting Oversight Board (PCAOB). Actions attributed to the PCAOB in this section shall be performed as authorized by the Sarbanes-Oxley Act of 2002 and the PCAOB's bylaws.

(b) Definitions. For the purposes of this section, the following definitions shall apply:

(1) Budget category means a grouping of similar expenditures within the PCAOB's budget. Budget categories shall include, among others: personnel, training, recruiting and relocation expenses, information technology, consulting and professional fees, travel, administrative expenses, lease costs and related expenses, and capital improvements of facilities.

(2) Budget justification means the justification for each annual budget, prepared in concise and specific terms, covering all of the PCAOB's programs and activities, and including, among other things as may be requested by the Commission:

(i) A performance budget for the budget year;

(ii) An analysis of the PCAOB's budget, including a tabular presentation that identifies the budgetary resources required for each program area (with a breakout of resources by budget category); a description of the budgetary resources identified in the budget in the context of the PCAOB's programs and activities; and an explanation of the analysis used to determine the resources needed to accomplish each program and strategic goal that demonstrates that reasonable opportunities for making more efficient and effective use of resources have been explored;

(iii) A description of the relationship between the results or outcomes the PCAOB expects to achieve (as discussed in the PCAOB's strategic plan) and the resources requested in the budget;

(iv) Assumptions underlying the calculation of the working capital reserve as permitted in paragraph (d)(3) of this section and assumptions underlying PCAOB estimates, including work years, program outputs, base compensation levels and proposed compensation increases, and costs of inputs such as materials or contract costs;

(v) A discussion of any models used to develop PCAOB estimates;

(vi) Detailed funding levels for education, training, and travel of the PCAOB workforce;

(vii) Information sufficient for the Commission to assess current and proposed capital projects and information technology projects; and

(viii) A statement that the PCAOB has considered relative costs and benefits in formulating the programs, projects and activities described in the budget.

(3) Budget year means the PCAOB fiscal year that is the subject of the budget prepared and submitted by the PCAOB to the Commission for approval.

(4) Current year means the PCAOB fiscal year that precedes the budget year, and is the year in which the PCAOB prepares the budget.

(5) Performance budget means a budget that presents what the PCAOB proposes to accomplish in the budget year and what resources these proposals will require, and that serves as the primary basis for the justification of the budget submitted to the Commission for approval. The performance budget includes:

(i) A description of what the PCAOB plans to accomplish, organized by strategic goal;

(ii) Background on what the PCAOB has accomplished, organized by strategic goal;

(iii) Analyses of the strategies the PCAOB uses to influence strategic outcomes, including whether those strategies could be improved and, if so, how they could be improved;

(iv) Analyses of the programs that contribute to each goal and their relative roles and effectiveness;

(v) Performance targets for the budget year and the current year and how the PCAOB expects to achieve those targets, as well as actual performance levels achieved in the year immediately preceding the current year;

(vi) The budgetary resources the PCAOB is requesting to achieve those targets;

(vii) Descriptions of the operations, processes, staff skills, information and other technologies, human resources, capital assets, and other resources to be used in achieving the PCAOB's performance goals; and

(viii) Descriptions of the programs, policies, and management, regulatory, and other initiatives and approaches to be used in achieving the PCAOB's performance goals.

(6) Preliminary budget means the draft budget submitted for initial consideration by the Commission, which shall be a complete or substantially complete budget for the budget year, and which is accompanied by a budget justification.

(7) Program area means the array of the budgeted amounts and other budget-related data according to the major purpose served, such as registration, inspection, standard-setting, enforcement, and administration.

(8) Receipts means collections that result from issuers' payments of accounting support fees; public accounting firms' payment of registration fees and fees associated with annual reports; interest income; and other sources of revenue.

(9) Strategic plan means the PCAOB's overarching plan for accomplishing its strategic goals, including forecasts for the current and four following years; estimates of the effect that reasonably foreseeable changes impacting the auditing profession and securities markets could have on program levels; and a discussion of the impact that program levels and changes in methods of program delivery, including advances in technology, could have on program operations and administration.

(10) Supplemental budget means a budget or amendment thereto submitted to the Commission for approval subsequent to Commission approval of the budget for the budget year, when:

- (i) There is a need for additional funds in a program area;
- (ii) Resources are to be applied in a manner not fairly implied in the Commission-approved budget and budget justification, such as when programs are

created to perform functions that are not, or to perform functions in a way that is not, fairly implied from the Commission-approved budget and budget justification; or

(iii) Programs described in the Commission-approved budget and budget justification are to be eliminated.

(c) Timetable. The timetable for preparation and submission of the annual budget is as follows:

<u>Date</u>	<u>Event</u>
On or before March 15	PCAOB provides a narrative of its program issues and outlook for the budget year
On or before April 30	Commission provides economic assumptions and general budgetary guidance to the PCAOB
On or before July 31	PCAOB submits preliminary budget and budget justification for Commission review
August – October	Consultation between Commission and PCAOB; Commission staff conducts review of PCAOB preliminary budget, budget justification and related information

On or before October 31	Commission passback of budget to the PCAOB with proposed revisions
On or before November 30	PCAOB adopts budget and submits it, along with the budget justification, to the Commission
On or before December 23	Commission votes on the PCAOB budget

(d) Contents of budget. (1) To facilitate Commission review and approval, each budget (including each preliminary budget and budget submitted for Commission approval) shall:

- (i) Be accompanied by a budget justification.
- (ii) Include information for the budget year, the current year, and the year immediately preceding the current year, regarding actual or projected spending by program area, receipts, debt, and employment levels.
- (iii) Be consistent with, or explain any deviations from, the economic assumptions and budgetary guidance provided by the Commission.
- (iv) Include statements of PCAOB programs, initiatives and strategies for the budget year.
- (v) Earmark each amount for a specific budget category within a program area.

(vi) Include planned beginning-of-year and end-of-year headcounts for each program area.

(2) Each budget submitted for Commission approval shall be consistent with the preliminary budget and any revisions proposed by the Commission when the budget was passed from the Commission back to the PCAOB or explain any changes from the preliminary budget and/or such proposed revisions.

(3) In addition to amounts needed to fund disbursements during the budget year, a budget may reflect receipts in amounts needed to fund expected disbursements during a period not to exceed the first five months of the fiscal year immediately following the budget year (the working capital reserve), provided such amounts shall be disbursed only as specified in the following year's budget or in a supplemental budget approved by the Commission.

(4) In approving the budget the Commission may not change the amounts earmarked for programs, program areas, or activities, or any other aspects of the budget; provided, that if the budget is conditionally rather than finally approved, then the Commission may transmit to the Board such proposed changes as are consistent with the preliminary budget and any revisions previously proposed by the Commission when it passed the budget back to the PCAOB. No proposed reduction or increase may be greater than that included in the preliminary budget and any revisions previously proposed by the Commission when it passed the budget back to the PCAOB.

(5) In the event the budget is conditionally approved by the Commission, the PCAOB shall have the opportunity to consider the changes proposed by the Commission and to vote again for final approval of the budget as amended. If this iterative process

has not resolved differences between the Commission and the PCAOB by December 23, then the terms of the most recent conditional approval shall become final, and the budget shall be deemed finally approved.

(e) Limitation on spending. (1) The PCAOB shall not spend in a budget year more than the amount specified in the Commission-approved PCAOB budget for that year, regardless of the source of the funds, unless such expenses have been approved by the Commission through a supplemental budget request.

(2) Funds may be disbursed by the PCAOB only in accordance with the Commission approved budget, provided however, during the budget year the PCAOB may transfer amounts totaling not more than \$1,000,000 into or out of each program area without prior Commission approval. Further, the PCAOB shall not:

(i) Apply its resources in a manner not fairly implied in the Commission-approved budget and budget justification, such as to create programs to perform functions that are not, or to perform functions in a way that is not, fairly implied from the Commission-approved budget and budget justification, or

(ii) Eliminate programs described in the Commission-approved budget and budget justification.

(3) In the event that the Commission has not approved a budget for a PCAOB fiscal year before the beginning of that fiscal year, the PCAOB may spend funds from the reserve and continue to incur obligations as if the PCAOB budget or supplemental budget most recently approved by the Commission were continuing in effect for that fiscal year.

(f) Supplemental budget. (1) The PCAOB may submit to the Commission a request for approval of a supplemental budget subsequent to Commission approval of the

budget for the budget year in order to spend any amounts in excess of, or contrary to, the limitations described in paragraphs (e)(1) and (e)(2) of this section.

(2) To facilitate Commission review and approval, a supplemental budget shall include:

(i) Detailed information regarding the impact of the supplemental budget on each affected program area, including costs by cost category, project or activity;

(ii) A statement regarding how the supplemental budget facilitates the strategic and policy goals of the PCAOB;

(iii) Information indicating why the amount was not included in the budget for the current year, including a description of any subsequent and unforeseen events or circumstances necessitating the supplemental budget request;

(iv) Information indicating why the request should not or can not be postponed until the next regular annual budget process; and

(v) The proposed source for the funds, including any offsets to be made elsewhere in the PCAOB's programs and activities.

(g) Maintenance of records; reports. (1) The PCAOB shall maintain, and make available to the Commission or Commission staff upon request, a strategic plan and records in reasonable detail that support each preliminary budget, budget, budget justification, supplemental budget and other report or communication in compliance with this section, including past and projected receipts, outlays, obligations, and employment levels.

(2) The PCAOB is required to maintain and, within 30 business days after the end of each fiscal quarter, to furnish to the Commission a report of its spending and

staffing levels for the quarter just ended, comparing those levels to the levels in the Commission approved budget.

(h) Publication of budget. (1) Following submission of the PCAOB-approved budget to the Commission, such budget and budget justification, subject to any applicable exemption under the Freedom of Information Act, shall be made available to the public. Neither the Commission nor the PCAOB shall publish a preliminary budget, budget, budget justification, or any underlying materials in connection therewith, until such time as the budget is approved by the PCAOB and submitted to the Commission for its approval.

(2) Supplemental budgets shall be made public, following approval by the PCAOB and submission to the Commission, in the same manner as described in paragraph (h)(1) of this section.

(3) The Commission-approved budget shall be made available to the public at the time of such approval.

(i) Waivers of rule provisions. The Commission, in its discretion, may waive compliance with any provision of this §202.11.

By the Commission.

Nancy Morris  
Secretary

July 18, 2006