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November 3, 2023

**SENT VIA EMAIL: [comments@pcaobus.org](mailto:comments@pcaobus.org)**

Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, NW  
Washington, DC 20006-2803

Re: Proposed Amendments to PCAOB Rule 3502 Governing Contributory Liability; PCAOB Rulemaking Docket Matter No. 053

Dear Office of the Secretary:

We appreciate the opportunity to share our views and provide input on the Public Company Accounting Oversight Board's ("PCAOB" or the "Board") Proposed Amendments to Rule 3502 Governing Contributory Liability (referenced herein as proposed Rule 3502, the proposed rule or the proposal).

Moss Adams LLP is the largest accounting and consulting firm headquartered in the western United States, with staff over 4,400, including more than 400 partners. Founded in 1913, the firm services public and private middle-market businesses, not-for-profit, and governmental organizations across the nation. We are an annually inspected Top 15 accounting firm in the US. We audit approximately 108 issuers, including 26 benefit plan issuers filing with the SEC on Form 11-K. Our desire is that our feedback will provide perspectives on the impact that the proposed amendments might have on audits of small and medium-sized entities.

We support the Board's efforts to evaluate how it can best structure its rules and enforcement program in a manner that will protect investors and improve audit quality. We are committed to promoting audit quality and appreciate that the Board's enforcement program plays a role in achieving that outcome.

We believe that any project to modify the framework by which auditors can be held liable for violations of PCAOB rules and standards should include a clear assessment of why that current framework exists and whether, in practical application, the current framework has impeded the PCAOB's effectiveness in bringing enforcement actions to fulfill its mission. This assessment should be performed considering all of the enforcement tools at the PCAOB's disposal and in light of the structure of other enforcement programs such as that of the U.S. Securities and Exchange Commission (SEC or Commission). That exercise is especially important in a situation like this one, where the Board in 2004 and 2005 considered, and then rejected, the negligence standard in the context of contributory liability that it is now proposing.

In our view, the current rule is effective. We share the views expressed in the Center for Audit Quality's letter dated November 2, 2023. In summary:

### **1. Adoption of the Proposed Rule Could Have Unintended Consequences by Negatively Impacting Audit Quality**

We are concerned that the proposal could exacerbate the accounting talent crisis. We believe there is a risk of inefficient and unproductive "self-protective" behavior that will occur if the amendments are approved. Further, the Proposal could have a negative impact on smaller firms and reduce the market for audit services.

We believe smaller firms may be at risk from any misallocation of resources that results from "self-protective" behavior, because highly talented individuals may resist practicing in areas subject to PCAOB Standards as they may perceive the risk as outweighing the opportunity. This would lead to fewer compensating resources to help ensure compliance with PCAOB rules and standards. In a market that has already experienced small to medium-size firms exiting the SEC space citing the burden of compliance with PCAOB regulations, a negligence standard for contributory liability could turn out to be a deciding factor in causing a broader exit by small and medium-size firms in the market for public company and registered broker-dealer engagements, thereby reducing competition and audit quality.

### **2. The Rationale for the Proposal Is Not Clear**

We are concerned the proposal does not have an adequate cost-benefit assessment, as noted below:

- The Commission already has the authority to sanction negligent conduct that contributes to another party's violations. The Board states that the Commission actually exercises this authority in practice to sanction negligent conduct and cites exclusively cases in which the Commission concluded that discipline of an associated person was appropriate under SEC Rule of Practice 102(e) or Securities Exchange Act of 1934 (Exchange Act) Section 4C, neither of which permits the Commission to charge a respondent based on a single instance of simple negligence. To the extent that the Board plans to charge single instances of simple negligence for contributory liability, then, it is proposing to wield a power that its analysis does not demonstrate the Commission having exercised, which causes concern about the costs and benefits that the Board articulates.
- It is difficult to predict what incremental enforcement might result from its adoption of a modified Rule 3502, which in turn presents notable challenges for a thorough cost-benefit analysis. The costs or the benefits of the Board's proposal have not been adequately assessed.
- The true costs and benefits of amendments to Rule 3502 cannot be known until the Board finalizes other proposed standards, especially its quality control proposal given the additional responsibilities and obligations that proposal would place on certain personnel at registered firms.

### **3. Individual Liability for Single Instances of Simple Negligence Would be Contrary to SEC Practice and Inappropriate**

The proposal would permit an individual or entity to be held liable not only directly for a single instance of negligence that violates a Board rule or standard, but also secondarily for a single instance of negligence that is not itself a violation but directly and substantially contributes to the violation of another.<sup>1</sup> Although the Board notes the SEC holds similar power under Exchange Act Section 21C,<sup>2</sup> its conclusion that the proposed modification of Rule 3502 would merely put the PCAOB on par with the SEC is unsupported.

### **4. The Legal Basis for a Contributory Liability Standard Based in Negligence Is Not Clear**

As with any Board action, a modification of Rule 3502 must rest on the foundation of the Board's statutory authority. In its 2005 release adopting Rule 3502, the Board cited two sources: its authority under Section 103 of Sarbanes-Oxley "to set ethical standards;"<sup>3</sup> and the authority "inherent in, and necessary to," the Board's enforcement authority under Sarbanes-Oxley Section 105.<sup>4</sup> However, in approving the Board's adoption of Rule 3502 in 2006, the Commission cited only Section 103 as the statutory basis.<sup>5</sup> In its current proposal, the Board appears to rely again on Sections 103 and 105, though its argument under Section 105 now appears to be that the Board is permitted—in general—to bring enforcement actions based on a single act of negligence.<sup>6</sup> Neither of these provisions provides a basis for the proposed rule.

### **5. The Board Should Consider Extending the Effective Date of Its Proposal**

We recommend that any modifications to Rule 3502 be implemented subsequent to the effective dates of other standards proposed but not yet adopted by the Board (or subsequent to a determination by the Board not to adopt those standards), and with additional analysis by the Board concerning the expected costs and benefits of its proposal in light of those standards.

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<sup>1</sup> Based on footnote 65, the Board even appears to imagine the possibility of tertiary liability, in which one associated person's conduct contributes to the conduct of a second associated person, which in turn contributes to a registered firm's violation. While the footnote appears to recognize that the first associated person's conduct would still have to meet the criteria of "directly and substantially" contributing to the ultimate firm violation, the mere mention of such a scenario suggests that the Board may intend to stretch the definition of "directly" beyond the bounds of common usage.

<sup>2</sup> See 15 U.S.C. § 78u-3(a).

<sup>3</sup> 2005 Adopting Release, pages 9-10.

<sup>4</sup> 2005 Adopting Release, page 12.

<sup>5</sup> See *Public Company Accounting Oversight Board; Order Approving Proposed Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees and Notice of Filing and Order Granting Accelerated Approval of the Amendment Delaying Implementation of Certain of these Rules*, SEC Rel. No. 34-53677 (Apr. 19, 2006) ("Proposed Rule 3502 establishes a standard of ethical conduct for persons associated with registered public accounting firms").

<sup>6</sup> Proposing Release, page 12 n.43. The Board also cites Sarbanes-Oxley Sections 101(c)(2), 101(c)(4), 101(c)(6), and 101(g)(1) for authority. See *id.* at 2 n.4. Those provisions speak to the Board's authority to sanction registered firms and associated persons, but not to the availability of contributory liability (let alone negligent contributory liability) as a permissible theory of violation.

We appreciate the opportunity to comment on the Proposed Amendments to PCAOB Rule 3502 Governing Contributory Liability. As the Board gathers feedback from other interested parties, we would be pleased to discuss our comments or answer any questions that the Board may have regarding the views expressed in this letter. If you require further information regarding our response, please contact Michael Spencer, Partner in our Professional Practice Group, at 408-916-0589 or by email at [Michael.Spencer@mossadams.com](mailto:Michael.Spencer@mossadams.com).

Sincerely,

*Moss Adams LLP*