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December 12, 2011

PCAOB Release No. 2011-006
PCAOB Rulemaking Docket Matter No. 37
Concept Release on Auditor Independence and Audit Firm Rotation

Dear Mr. Seymour:

We are members of the Corporate Governance and Board Advisory practice group of Cravath, Swaine & Moore LLP, and in that capacity spend a significant amount of time working with the audit committees of numerous public companies, as well as with other board committees, full boards of directors, and members of senior management.¹ We are submitting this letter in response to the Board's request for public comment on its Concept Release concerning auditor independence and audit firm rotation.

We share the Board's commitment to auditor independence, which we believe is of critical importance to the efficient and effective functioning of our capital markets. We question, however, whether audit firm rotation would accomplish the Board's goal of promoting independence in a reliable manner, if at all. More importantly, we believe that such a policy would impose tremendous costs and inefficiencies that would far outweigh the intended benefits. These costs and inefficiencies have been thoroughly described in a substantial number of thoughtful comment letters already received by the Board from a variety of sources, including many letters on behalf of public company audit committees.

Rather than repeat the arguments made in those letters, we wish to briefly note the larger corporate governance context within which the question of auditor independence properly should be analyzed. Independence, after all, is not an end in itself, but a means of promoting both audit quality and -- most critically -- investor

¹ The views expressed in this letter, however, are strictly our own and not submitted on behalf of any of our audit committee or other clients.

confidence in public companies and public markets. It is our belief that mandating the automatic rotation of audit firms would be inconsistent with the fundamental governance framework on which securityholders and other market participants have come to rely, and would thereby damage rather than enhance investor confidence.

The Board is of course familiar with the Sarbanes-Oxley Act, which was enacted in 2002 in response to the infamous accounting frauds at Enron and WorldCom, which called into question the reliability and integrity of public company financial statements and the audits that were being performed on those statements. It is fair to say that those events truly resulted in a “crisis” of confidence among investors and other market participants, and that the Sarbanes-Oxley Act was the legislative response to that crisis. Along with creating the Board itself to regulate the accounting profession, Sarbanes-Oxley ushered in a new era of corporate governance. In what was a radical departure from the established corporate order, under which boards played only a secondary/supervisory role in the operation of public corporations in accordance with state law, primary responsibility for selecting the audit firm and overseeing the company’s relationship with that firm was transferred from management to audit committees consisting solely of independent board members. In our view, this aspect of Sarbanes-Oxley has been an unqualified success from the perspective of improving audit quality and generating and maintaining investor confidence in the integrity of financial statements. The past decade has seen the development of dramatically stronger audit committees that are more expert with respect to accounting and finance matters; more independent of management; more actively involved in safeguarding the accuracy and reliability of their companies’ financial statements and internal controls; and more directly and vigorously policing the quality of external audits. While there will always be room for improvement, and there will always be the occasional spectacular audit failure, the crisis in investor confidence in the integrity of financial reporting by public companies was in fact resolved by the reforms imposed by Sarbanes-Oxley, and in particular by the empowerment of audit committees. As a group, the independent directors who serve on those committees have fully accepted the new responsibilities conferred on them by Congress in 2002 and have carried out their duties in a diligent, informed and effective manner.

If the Board were now to mandate the rotation of audit firms, the effect necessarily would be to reverse a fundamental premise of, and arguably the greatest achievement brought about by, the Sarbanes-Oxley Act. To take oversight authority away from the individuals who are best positioned (and legally obligated as fiduciaries) to exercise professional skepticism by assessing a particular audit relationship and ensuring that it is independent in fact as well as in appearance, and to instead impose a one-size-fits-all rule, can only be interpreted as a powerful statement by the Board that audit committees cannot be relied upon to ensure that their companies’ auditors are independent. In addition to all the more tangible costs and other considerations that have been advanced by other commentators who believe rotation would not be effective, we urge the Board to consider whether sending that message -- that audit committees are not to be trusted to make the necessary judgments relating to auditor independence -- is either justified by objective evidence or likely to achieve the Board’s intended objective of improving audit quality and investor confidence. Occasional anecdotes notwithstanding,

we are not aware of credible evidence that audit committees are not capable of exercising the responsibilities that already have been conferred upon them, and believe instead that there is compelling evidence to the contrary. For the Board effectively to state otherwise in such a broad and unqualified manner would undermine rather than foster the Board's ultimate objective of promoting investor confidence, and thereby do unnecessary damage to those who rely on financial statements issued by reporting companies.

We thank the Board for this opportunity to comment, and we would be pleased to provide any further comment or input that the Board would find helpful.

Very truly yours,



Marc S. Rosenberg
Susan Webster
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