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July 8, 2013

Ms. Phoebe W. Brown
Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

Re: PCAOB Proposed Auditing Standard—Related Parties, Proposed Amendments to Certain PCAOB Auditing Standards Regarding Significant Unusual Transactions, and Other Proposed Amendments to PCAOB Auditing Standards (PCAOB Release No. 2013-004, May 7, 2013, and PCAOB Rulemaking Docket Matter No. 038)

Dear Ms. Brown:

The U.S. Chamber of Commerce (the “Chamber”) is the world’s largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness (“CCMC”) to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy. The CCMC believes that businesses must have a strong system of internal controls and recognizes the vital role external audits play in capital formation. The CCMC supports efforts to improve audit effectiveness and appreciates the opportunity to comment on the Public Company Accounting Oversight Board (“PCAOB”) *Proposed Auditing Standard—Related Parties, Proposed Amendments to Certain PCAOB Auditing Standards Regarding Significant Unusual Transactions, and Other Proposed Amendments to PCAOB Auditing Standards* (“the Proposal”).

We commend the PCAOB’s consideration of the comments on the February 2012 exposure draft and taking action to addressing some of those issues. However, not all of our concerns are fully addressed in the Proposal and we have attached our

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previous comment letter to reiterate these issues for the record. Additionally, this letter will further elaborate our concerns regarding the Proposal.

Discussion

The Proposal is the second time the PCAOB has released for comment a proposed auditing standard on related parties and proposed amendments on auditing significant unusual transactions and financial relationships and transactions with executive officers. The PCAOB received 37 comment letters on the initial exposure draft issued in February 2012. The CCMC provided comments on the initial exposure draft.¹

I. Cost Benefit Analysis

The PCAOB's February 2012 exposure draft did not contain a cost-benefit analysis. Thus, the CCMC's letter of May 30, 2012 noted:

[T]hat commenters are therefore unable to ascertain what the estimated costs are and the burdens that will be placed upon businesses and auditors as a result of the Proposal. This inhibits the ability of commenters to provide the PCAOB with a fully informed analysis that could lead to beneficial changes in the Proposal.

The Proposal recognizes that the 2012 Jumpstart Our Business Startups Act (JOBS) now makes economic analysis a necessary pre-condition for applying new PCAOB auditing standards to an audit of any emerging growth company (EGC). Specifically, JOBS Section 103(a) (3) requires that rules adopted by the Board after the date of enactment of JOBS shall not apply to an audit of any EGC, unless the Commission determines that the application of such additional requirements is necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation.

¹ See the May 30, 2012 letter from the United States Chamber of Commerce Center for Capital Markets Competitiveness on the PCAOB *Proposed Auditing Standard – Related Parties, Proposed Amendments to Certain PCAOB Auditing Standards Regarding Significant Unusual Transactions, and Other Proposed Amendments to PCAOB Auditing Standards* (PCAOB Release No. 2012-001, February 28, 2012 and PCAOB Rulemaking Docket Matter No. 038).

The CCMC recognizes that one reason the PCAOB issued this second exposure draft is to solicit information on the estimated costs and burdens that will be placed upon businesses and auditors as a result of the Proposal, and to solicit other information on how the Proposal would contribute to investor protection and promote efficiency, competition, and capital formation. For example, of the 50 questions included in the Proposal on which the Board requests comments, at least 24 relate to economic considerations, including audits of EGCs.

Further, the CCMC recognizes that the Proposal does not represent a final standard. Thus, additional evidence and analysis will need to be collected and analyzed any ensuing standard adopted by the Board and submitted for approval by the Securities and Exchange Commission (“SEC”).

Nonetheless, given the information available in the Proposal, in particular information in Section IV on “Economic Considerations, Including Audits of Emerging Growth Companies,”² the CCMC has concerns about elements of the PCAOB’s approach to economic analysis and the nature and substance of that analysis.

The Proposal includes a number of assertions as part of the PCAOB’s economic analysis.³

² See page A4-96 through A4-117 in the Proposal.

³ As an example, the following assertions can be found on pages A4-96, A4-97, A4-99 and A4-104 of the Proposal:

- The proposed auditing requirements *have the potential* to enhance audit quality in ways that could also enhance the quality of a company’s financial reporting and, therefore, they *could*:
 - Reduce information asymmetry between companies and investors because they *may*
 - improve the auditor’s identification and assessment of risks of material misstatement of financial statements and response to those risks, which *may* lead to higher quality accounting and disclosures for investors
 - result in a more meaningful exchange of information between the auditor and a company’s audit committee
 - Reduce the cost of capital for issuers
- The Proposal reflects a risk-based and scaled approach because the audit procedures performed and, therefore, the associated costs are commensurate with the risks of material misstatement
 - Thus, companies *without* extensive relationships or transactions with related parties, significant unusual transactions, or financial relationships and transactions with the company’s executive officers would not be expected to incur a significant change in audit costs
- The Proposal is necessary to align PCAOB auditing standards on transactions and relationships with related parties, significant unusual transactions, and relationships and transactions with executive officers with the PCAOB’s suite of risk assessment standards (AS 8 through AS 15)
- Other auditing standards-setters have revised their requirements on related parties, for example:
 - The International Auditing and Assurance Standards Board (“IAASB”) issued a revised standard in July 2008
 - The Auditing Standards Board (“ASB”) issued a revised standard in October 2011

Many of these assertions are generic or speculative and are not linked to the elements of the Proposal. In fact, they could be made for almost any proposed auditing standard regardless of topic or substance. It appears to the CCMC, therefore, that the Proposal fails to explicitly articulate any appropriate economic baseline against which to measure the proposed requirements likely economic impact.

The CCMC appreciates that the Proposal does attempt to reference various types of evidence as support for revising audit standards, but fails to provide specifics for how it relates to the Proposal itself.⁴

The Proposal states that the PCAOB determined 579 SEC registrants have identified themselves as EGCs as of November 15, 2012. This number is up from the 196 EGCs noted in the PCAOB's economic analysis for AS No. 16, *Communications with Audit Committees*, sent to the Commission on August 28, 2012. The Proposal provides some general descriptive data about EGC's, which reveal that EGCs are a diverse group and generally appear to be companies new to the SEC reporting process.⁵ Based on these data, the Proposal briefly suggests qualitative-type conjectures related to information asymmetry, investor confidence, competition, and costs. However, the Proposal contains no substantive analysis of the economic impact of the proposed requirements on EGCs, EGCs vis-à-vis other companies, or

⁴ For example see the following that can be found at page 5, A4-96, A4-98, A4-99, A4-114, of the Proposal:

- An analysis of alleged audit failures from 1997-2003 by the Quality Control Inquiry Committee largely involves cases before The Sarbanes-Oxley Act of 2002 ("SOX") and before a number of other legislative, regulatory, and standard-setting actions over the last decade.
- General references to instances of fraudulent financial reporting involving related party transactions, significant transactions outside the normal course of business, and transactions and relationships with executives include cases prior to SOX and prior to the promulgation of revised auditing standards such as Statement of Auditing Standard No. 99 on *Consideration of Fraud in a Financial Statement Audit* (December 15, 2002).
- References to two PCAOB 4010 reports on inspection results from 2004-2006 and 2007-2010 for tri-annually inspected audit firms issued February 25, 2013 and October 22, 2007, respectively, report that inspection deficiencies involved related parties, but the Proposal
 - Does *not* provide any specificity about the number of instances;
 - Does *not* discuss any root cause analysis in order
 - To rule out that the observed deficiencies related to problems with auditor performance;
 - To provide support that the observed deficiencies related to gaps in auditing standards and the proposed requirements would address these identified deficiencies.
- Settled SEC enforcement actions and PCAOB disciplinary actions to date which, by their very nature, would seem to indicate auditor performance problems rather than gaps in auditing standards.

⁵ See pages A4-112 through A4-115 in the Proposal. The Proposal also reports that a review of 450 audited financial statements from a self-identified sample of EGCs indicates that 54 percent disclosed at least one related party transaction (see footnote 94 on page A4-115 in the Proposal)

companies generally, although the CCMC appreciates that the Proposal does request commenters views and empirical evidence on these issues.⁶

Finally, the Proposal does not adequately address potential alternatives to the proposed requirements. The CCMC appreciates that the Board issued Staff Audit Practice Alert No. 5, *Auditor Considerations Regarding Significant Unusual Transactions* (April 7, 2010) (“Staff Alert”) before deciding to issue its initial proposal. However, the Proposal fails to discuss or provide evidence on why this Staff Alert was inadequate.

As another example of the lack of evidence on the consideration of potential alternatives, the PCAOB provides a comparison of significant differences among the objectives and requirements of this Proposal versus other analogous standards of the IAASB and ASB.⁷ However, this comparison contains no analysis of or rationale for why the PCAOB chose not to converge the proposed auditing requirements with those of the IAASB and ASB. As a result, the Proposal adds to audit complexity and raises doubt that the proposed requirements would be cost/benefit effective.

II. CCMC Recommendation

The CCMC appreciates that the PCAOB faces challenges in doing economic analysis for auditing standards. However, the concerns just discussed suggest that all stakeholders would be well served if the PCAOB would reconsider its approach to economic analysis.

The CCMC suggests that the PCAOB needs an appropriate and transparent framework for economic analysis—one that will serve as a template for such analysis across all PCAOB rulemaking initiatives. One example of such a framework is the SEC staff memorandum, “Current Guidance on Economic Analysis in SEC Rulemakings” dated March 16, 2012.

Thus, the CCMC recommends that the PCAOB develop guidance on economic analysis for PCAOB rulemaking. Once developed, the PCAOB should expose the framework for public comment and the finalized framework should be

⁶ See page A4-115 in the Proposal.

⁷ See Appendix 5 in the Proposal.

publicly disclosed. As a starting point, the PCAOB could consider adapting the framework in the SEC staff memorandum to an audit context.

III. Other Matters

Similar to the prior exposure draft, the Proposal includes proposed amendments to existing PCAOB auditing standards that would add requirements for auditors to perform procedures to obtain an understanding of the company's financial relationships and transactions with its executive officers, including executive compensation. The intent of this added requirement is to assist the auditor in identifying and assessing risks of material misstatement—not to call into question the policies and procedures of the company. However, the CCMC previously expressed concern that media coverage of the proposed amendments indicated that the PCAOB's intent was not well understood and that an expectation gap was being created.

We appreciate that the PCAOB acknowledged this problem and revised the wording of the proposed amendment to paragraph 10A of Auditing Standard No. 12, *Identifying and Assessing Risks of Material Misstatement*. This revision partially reflects wording suggested in our previous comment letter. Notwithstanding this revision, we continue to recommend that the PCAOB include more expansive language in the standard itself to provide clarity on intent and to avoid problems down the road. The language recommended in our prior letter, including a statement that “these audit procedures are not intended to call into question the policies and procedures of the company ...,” could be added as a note to paragraph 10A.

Finally, the Proposal now states that the Board anticipates the proposed standard and proposed amendments would be effective for audits of financial statements for fiscal years beginning on or after December 15, 2013. This proposed effective date is not unreasonable as long as the PCAOB adopts and the SEC approves a final standard before the end of 2013.

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Conclusion

Once again, the CCMC appreciates the opportunity to comment on the Proposal. Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

A handwritten signature in black ink, appearing to read 'T. Quaadman', with a long horizontal flourish extending to the right.

Tom Quaadman