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April 4, 2003

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 001

Dear Sir or Madam:

This letter is submitted on behalf of the Committee on Law and Accounting of the American Bar Association's Section of Business Law (the "Committee") in response to the request by the Public Company Accounting Oversight Board (the "Board") for written comments on its proposed registration system for public accounting firms (the "Proposal"). The Board issued the Proposal in response to Section 102(a) of the Sarbanes-Oxley Act of 2002 (the "Act"), which states that public accounting firms must register with the Board within 180 days of the date on which the Securities and Exchange Commission (the "Commission") determines that the Board is capable of fulfilling its responsibilities under the Act.

The comments expressed in this letter represent the views of the Committee only and have not been approved by the American Bar Association's House of Delegates or Board of Governors and therefore do not represent the official position of the Association. In addition, this letter does not represent the official position of the ABA Section of Business Law, nor does it necessarily reflect the views of all members of the Committee.

Various members of our Committees represent public accounting firms, and some members represented clients in connection with the legislative activity that led to the Act. In preparing this comment letter, we have directed our comments to issues on which we have professional expertise.

## I. General Comments

Section 102(b) of the Act establishes a series of specific requirements for the contents of registration forms that public accounting firms will be required to file with the Board. Within this framework, however, the Board has considerable discretion to specify the level of detail required in registration forms filed by public accounting firms.

The Committee supports the establishment of a registration system and believes that the Board's registration system should be designed to ensure that accounting firms - whether within or outside the United States - that audit SEC-registered issuers are both equipped to provide audit services and subject to effective Board oversight. At the same time, the Committee urges the Board to minimize the burdens imposed on accounting firms under the registration process and to recognize that accounting firms located outside the United States may face unique challenges in complying the Board's proposals.

We set forth below our comments with respect to specific aspects of the Board's proposed registration system.

## II. Specific Observations

### A. Standard for Approving Registration

The Board's proposed registration system consists of nine rules and a new Form 1. Under proposed Rule 2105(a), the Board will determine whether approval of an application for registration is consistent with the Board's responsibilities under the Act to "protect the interests of investors and to further the public interest in the preparation of informative, accurate, and independent audit reports for companies the securities of which are sold to, and held by and for, public investors."

While the Committee believes that this is an appropriate standard, it is also quite open-ended. Insofar as the consequences to an SEC registrant would be quite significant if the Board were to decline to register its accounting firm, or another firm that had played a "significant role" in its annual audit, we urge the Board to provide additional guidance as to the types of factors that might lead the Board to exercise its discretion and decline to approve a registration application.

### B. Withdrawal of Applications

Although proposed Rule 2105 establishes a timetable pursuant to which the Board would act on a registration application, it does not set forth procedures for an applicant to withdraw a pending registration application. There are circumstances, however, in which a public accounting firm might desire to withdraw or defer its application to register with the Board. For example, subsequent to the filing of an application with the Board, but prior to the Board's acting on the application, a firm might cease to audit or play a significant role in the audit of any SEC registrants. Another example of a situation where a firm might seek to withdraw its registration application might occur if the Board were to advise the applicant that it was not prepared to extend confidential treatment to portions of the firm's application pursuant to proposed Rule 2300.

While the Committee believes that the proposed rules would allow the Board to permit a public accounting firm to withdraw a pending registration application, we recommend that the rules expressly establish a procedure for a firm to notify the Board that it is withdrawing a pending application prior to Board action on the application.

C. Fee Disclosures

Parts II and III of Form 1 require applicants to provide a considerable amount of fee-related information to the Board, both with respect to each SEC-registered audit client (an "Issuer") and generally.

The proposed fee disclosures relating to specific Issuers are set forth in proposed Part II of Form 1. This section of the Form would require the disclosure of fees received by a public accounting firm from each Issuer during both the preceding and current calendar year for audit services, other accounting services, tax services and all other non-audit services. Each of the terms "audit services," "other accounting services" and "tax services" is defined in the Board's proposed rules. These definitions are similar to, but vary in important respects from, the fee disclosure categories contained in the Commission's recently amended auditor independence rules, which govern the disclosures required in proxy statements or annual reports filed by Issuers with the Commission.[1]

In particular, the Board stated that its proposed definition of "audit services" is intended to capture "the same category of services for which fees were required to be disclosed as 'audit fees' pursuant to the Commission's *2000* proxy disclosure rules" (emphasis added). The Board proposes to define "other accounting services," in turn, to capture "two categories of services: 1) services the fees for which are to be disclosed as 'audit fees' under the Commission's revised rules, but that were not previously disclosed as 'audit fees,' and 2) services the fees for which are to be disclosed as 'audit-related fees' under the Commission's revised rules." As a result, the Board's proposed definitions of fees for "audit services" and "other accounting services" would differ from the Commission's definitions of "audit fees" and "audit related fees," as amended earlier this year.

It is unclear whether these differences were intentional or inadvertent. For example, the Board's release states that "the Board has, to the extent possible, used concepts from the fee disclosures required of issuers by the Commission as part of its recent revisions to its auditor independence rules." This language suggests that the Board intended to model its fee disclosure categories after those contained in the Commission's revised rules. As noted, however, the actual fee disclosure categories proposed by the Board differ in various respects from the Commission's revised definitions.

Absent clarification, registered public accounting firms would have to track fees for services rendered to Issuers separately for purposes of (1) registration with (and, presumably, periodic reporting to) the Board and (2) providing information to Issuers for inclusion in their

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[1] Strengthening the Commission's Requirements Regarding Auditor Independence, Exchange Act Release No. 34-47265 (Jan. 28, 2003) (to be codified at 17 C.F.R. pts. 210, 240, 249, 275).

proxy statements filed with the Commission. In our view, such separate categories are not required under the Act and would impose an unnecessary burden on public accounting firms. Accordingly, we recommend that the Board revise its proposed fee disclosure categories to parallel those set forth in the Commission's revised independence rules.

In addition, Part III of proposed Form 1 would require accounting firms seeking to register with the Board to state their total revenues, whether or not derived from services rendered to Issuers, in the most recently completed fiscal year for audit services, other accounting services, tax services and all other non-audit services. As noted above, the Board's definitions of the various service categories differ from the definitions set forth in the SEC's current independence requirements. Moreover, some firms may be unable or find it quite burdensome to furnish such information to the Board for prior fiscal periods, particularly with respect to services rendered to clients that are not Issuers. Accordingly, while the Board might require firms that can readily assemble such data to include it in their registration applications (subject, of course, to Board procedures for requesting confidential treatment of proprietary information), we believe that the Board should also allow firms to report such data using alternative revenue categories, so long as they provide an explanation of the differences between the revenue categories that they are using and the Board's categories in their applications.

D. Issues Affecting Foreign Accounting Firms

Firms located outside the United States, however, may face unique challenges in complying the Board's registration requirements, particularly where they conflict with obligations or restrictions imposed on the firms under the laws of foreign jurisdictions. The Board's release indicates that the Board is sensitive to such considerations, and we support the Board's decision to convene a roundtable meeting on March 31, 2003 to obtain additional information regarding the impact of Board registration and oversight on foreign public accounting firms. We urge the Board to give careful consideration to comments received during the roundtable session and have identified below some of the issues that we believe merit additional consideration.

*Registration of Foreign Accounting Firms that Do Not Issue or Prepare Audit Reports on Issuers.* The Board proposes to exercise its discretion under the Act to require the registration not only of foreign accounting firms that issue or prepare audit reports on Issuers, but also those non-U.S. firms that play a "substantial role" in the preparation or furnishing of such reports with respect to Issuers. Proposed Board Rule 1001(n) would establish two quantitative tests for determining whether a firm had played a "substantial role" in the preparation or furnishing of an audit report.

While foreign accountants that participate in the audit of U.S. public companies may already be subject to various U.S. requirements, the Board has proposed, for the first time, that foreign accounting firms register with a single U.S. regulator, as condition to preparing, issuing or playing a substantial role in the preparation or issuance of audit reports on Issuers. As a practical matter, we believe that the Board should consider deferring any requirement for foreign accounting firms that do not themselves issue or prepare audit reports for Issuers to register with the Board, until it has gained experience administering the Act's registration, periodic reporting

and oversight requirements with respect to those foreign accounting firms that must register under the Act. Deferring the registration of such other firms at the present time would allow the Board to "fine tune" its requirements before extending them to a broader universe of foreign accounting firms, but would not prevent the Board from requiring such firms to register, or comply with other Board requirements, at a later date. Moreover, it would allow the Board to focus its resources at this early stage of its operations on those accounting firms that play a more significant role in the audits of Issuers.

*Listings of Disciplinary Proceedings*. Part V of Form 1 would require public accounting firms to disclose information relating to prior or pending criminal, civil governmental, private civil or administrative and disciplinary actions against the firms or their "associated persons" that involve conduct in connection with an audit report. While the primary focus on only audit-related proceedings is consistent with Section 102(b)(2)(F) of the Act, compliance with the Board's proposed requirements may pose special challenges for foreign public accounting firms.

For example, in some jurisdictions, a prior or pending administrative or disciplinary proceedings against an accounting firm or one of its employees may be considered confidential or non-public. In such situations, a required disclosure of the proceeding in a Board registration statement may contravene foreign law. We urge the Board to gather additional information regarding the likelihood of such conflicts before finalizing its registration requirements.

In other situations, the proposed disclosures would be difficult for foreign accounting firms subject to registration to interpret. In particular, proposed Item 5.5(a)(3) of Form 1 would require an applicant to disclose whether it, or any of its proprietors, partners, principals, shareholders or officers, had been a party to a case or proceeding, not otherwise disclosed pursuant to the Board's requirements, in which such person:

> was, in the previous ten years, convicted of any felony or misdemeanor, or of a substantially equivalent crime however denominated under the laws of a non-U.S. jurisdiction, arising out of such person's conduct as an accountant or that * * * involves the violation of section 152, 1241, 1342, 1343, 1348, 1349, 1512, 1513, 1519, 1520 or chapter 25 or 47 of title 18 of the United States Code or a violation of a substantially equivalent non-U.S. statute.

To comply with this complex requirement, a foreign firm, at a minimum, would need to (1) familiarize itself with a host of U.S. statutory requirements, (2) attempt to identify all foreign laws that were "substantially equivalent" to the U.S. requirements, (3) determine whether either the firm or any of its "associated persons" had violated any of the foregoing laws over the past 10 years and (4) evaluate whether the disclosure of any such proceedings would implicate any privacy or confidentiality laws under the laws of non-U.S. jurisdictions. In our view, this would likely impose a significant burden on foreign accounting firms. Accordingly, we recommend that the Board provide a clearer explanation as to the types of non-U.S. legal proceedings that it believes should be disclosed in a foreign accounting firm's registration statement pursuant to Item 5.5.

*Consents of Associated Persons.* The Board has proposed in Part VIII of Form 1 that public accounting firms registering with the Board must both consent to cooperate in and comply with any request for testimony or the production of documents made by the Board pursuant to its statutory authority and responsibilities under the Act and agree to secure and enforce similar consents from each of its "associated persons" as a condition of his or her employment or other association with the firm.

This requirement is generally consistent with Section 102(b)(3) of the Act. We would urge the Board, however, to recognize that laws in some countries may limit the ability of accounting firms to obtain or enforce consents of their employees to cooperate with a request from a regulator in another country for testimony or documents. In particular, a requirement that an accounting firm condition an employee's initial or continued employment on his or her willingness to provide information to the Board may violate labor or employment laws in some jurisdictions.

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We appreciate the Board's consideration of the Committee's comments. Members of the Committee would be pleased to meet with representatives of the Board to discuss our comments.

Respectfully submitted,

Thomas L. Riesenberg, Chair
Committee on Law & Accounting

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