



PCAOB Release No. 2003-005

STATEMENT REGARDING THE ESTABLISHMENT OF
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The Board has also proposed PCAOB Rule 3100 and a related definition that would appear in Rule 1001. Rule 3100 would require all registered public accounting firms to adhere to the Board's auditing (and related attestation), quality control, and ethics standards, and its independence rules, in connection with the preparation or issuance of any audit report for an issuer (as defined in the Act). Neither Rule 3100, Rule 3700, nor any professional standard or rule adopted by the Board will take effect until approved by the Securities and Exchange Commission ("Commission") pursuant to Section 107 of the Act.

Public

Comment: This release invites comment on the proposed rules herein. Interested persons may submit written comments to the Board. Such comments should be sent to Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments may also be submitted by e-mail to comments@pcaobus.org or through the Board's website at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 004 and should be received by the Board no later than 5:00 PM (EST) on May 12, 2003.

Board

Contact: Gordon Seymour, Acting General Counsel (202/207-9034; seymourg@pcaobus.org).

Section 103(a)(1) of the Act directs the Board to establish auditing and related attestation standards, quality control standards, and ethics standards to be used by registered public accounting firms in the preparation and issuance of audit reports, as required by the Act or the rules of the Commission, or as may be necessary or appropriate in the public interest or for the protection of investors. Similarly, Section 103(b) authorizes the Board to establish such rules as may be necessary or appropriate to implement the auditor independence requirements in, or as authorized under, Title II of the Act. While Section 103(a)(4) directs the Board to convene such expert advisory groups as may be appropriate to aid in standards-setting, it nevertheless affords the

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Board considerable discretion in determining the procedures by which it will develop and adopt Professional Auditing Standards.^{1/} Among other things, for example, it authorizes, but does not require, the Board to designate or recognize Board advisory groups or professional groups of accountants to propose standards to the Board.

This release describes the general process the Board intends to follow in establishing Professional Auditing Standards. As set forth in more detail below, the Board will convene an advisory group to assist it in performing its standards-setting responsibilities. The Board also intends to solicit public comment, and, where appropriate, to convene hearings or roundtable meetings, in order to obtain the views of issuers, accountants, investors, and other interested persons with respect to proposed Professional Auditing Standards. In this regard, the Board welcomes input and advice from established professional bodies and intends to include practicing accountants among the members of its advisory groups. The Board has, however, determined not to exercise its authority to designate any professional group of accountants as a formal participant in the Board's standards-setting process at this time.

This release also announces the proposed adoption of PCAOB Rule 3100 (and a related definition) and Rule 3700 and invites public comment thereon. If adopted, Rule 3100 would require all registered public accounting firms to adhere to the Board's auditing (and related attestation), quality control, and ethics standards, and its independence rules.^{2/} Rule 3700 would address the formation, composition, and other

^{1/} The auditing and related attestation standards, quality control standards, and ethics standards over which the Board has authority under Section 103(a) of the Act, and the independence rules the Board is authorized to adopt under Section 103(b), are collectively referred to in this release as "Professional Auditing Standards." This term is defined in proposed Rule 1001(p)(iv). The proposed definition is similar to that portion of the definition of the term "professional standards" that appears in Section 2(a)(10)(B) of the Act.

^{2/} As discussed below, in accordance with Section 103(a)(3)(B) of the Act, the Board is issuing a separate release concerning the initial, transitional adoption of certain existing auditing, quality control, and other standards, pending Board review of

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basic matters concerning the advisory group convened to aid in the Board's standards-setting process.

A. Adoption of New or Amended Professional Auditing Standards

Consistent with Section 103(a) of the Act, new Professional Auditing Standards will be established – and existing standards will be changed – only by Board rulemaking.^{3/} While, as discussed below, the Board will consider proposed new or amended Professional Auditing Standards recommended to it by other persons, no such proposed rule will become a standard of the Board unless adopted by the Board through rulemaking. The Board's authority with respect to Professional Auditing Standards will take effect as of the date on which the Commission determines, pursuant

those standards. These transitional standards are collectively referred to in this release as "Interim Professional Auditing Standards." Unless modified by the Board, any standard adopted as an Interim Professional Standard has the same effect as any other Professional Auditing Standard, and registered public accounting firms will be subject to the same obligation to comply with the interim standards while they are in effect as with the permanent standards.

^{3/} See also Report of the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, on S. 2673, S. Rep. No. 107-205 (July 26, 2002) ("The Committee has concluded that the Board's plenary authority in this area is essential for the Board's effective operation, a position taken during the hearings by a number of witnesses. . . ."). Board rules adopting or modifying Professional Auditing Standards, like all Board rules, become effective only upon approval by the Commission. In addition, the Board recognizes that the Commission may also establish professional standards applicable to accountants that practice before it and audit reports filed with it and that the Commission has the authority to institute proceedings to amend the Board's rules, including those that establish Professional Auditing Standards. See Sections 2(a)(10), 3(c)(2), and 107(b)(5) of the Act.

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to Section 101(d) of the Act, that the Board is so organized as, and has the capacity, to carry out the requirements of Title I of the Act and to enforce compliance therewith.

As a corollary to the Board's exclusive, statutory authority to establish and amend Professional Auditing Standards, all public accounting firms that are registered with the Board must comply with the Board's standards. While this requirement is implicit in the Act, the Board proposes to codify the obligation of registered firms to comply with the Board's standards in proposed Rule 3100. Any registrant that fails to adhere to the Board's Professional Auditing Standards will be subject to Board disciplinary proceedings in accordance with Section 105 of the Act.^{4/}

The Board invites comment on proposed Rule 3100 and the related definition. In particular, the Board seeks views on whether there are other standards, in addition to the Board's Professional Auditing Standards, with which the Board should require registered firms to comply.

B. Procedure for the Adoption of New or Amended Professional Auditing Standards

While the Board will, by rule, establish Professional Auditing Standards, it recognizes that the development of such standards should be an open process in which the accounting profession, the preparers of financial statements, the investor community, and others have the opportunity to participate. The Board encourages proposals and recommendations concerning Professional Auditing Standards. As discussed below, in order to facilitate the input and advice of a broad range of experts, the Board intends to form one or more advisory groups to assist it in standards-setting. In addition, the Board's staff will, of course, be actively involved in this process.

^{4/} In addition, the Act provides that any violation of the Board's rules is to be treated for all purposes in the same manner as a violation of the Securities Exchange Act of 1934, 15 U.S.C. 78a et seq., or the rules and regulations issued thereunder and any person violating the Board's rules "shall be subject to the same penalties, and to the same extent, as for a violation of [the Exchange] Act or such rules or regulations." Section 3(b)(1) of the Act.

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The Board envisions that proposed new Professional Auditing Standards, and changes to such standards, may arise from three sources:

- The Board, with the advice of its staff, may propose a new standard or a change to an existing standard.
- The Board advisory group (or recognized sub-group thereof), or a Board-appointed task force, may recommend to the Board that it propose a new standard or a change to an existing standard.
- Any other person or group may petition the Board and request that it propose a new standard or a change to an existing standard.

In the case of recommendations concerning Professional Auditing Standards that emanate from persons and groups other than the Board and its staff, the Board will consider the recommendation and, consistent with Section 103(c)(2) of the Act, decide, in a timely manner, whether or not to propose the standard in question either as recommended or with modifications.^{5/} In considering such a recommendation, the Board may decide to convene a standards development project by submitting the recommended standard or change to an existing standard to its development process. First, the Board may choose to direct its staff, an ad hoc task force, or both to analyze and evaluate the recommended standard. Next, with Board approval, the analysis and evaluation by the Board's staff (or task force) may be submitted to the advisory group

^{5/} The Board will encourage recommendations from outside persons to contain: (1) a clear description of the perceived problem or issue that the recommended new standard, or recommended change to an existing standard, seeks to address; (2) a clear explanation of how the recommended new standard, or recommended change to an existing standard, directly relates to the perceived problem or issue; and (3) the identity, area(s) of expertise, and appropriate contact information for the person submitting the recommendation. If the Board determines not to act on a recommendation, it may or may not notify the recommender or make a public announcement, depending on the circumstances.

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(or, if established, a recognized sub-group of an advisory group) for consideration. Recommendations or comments from an advisory group (or, if established, a recognized sub-group of an advisory group) would then be submitted to the Board, or staff of the Board designated by the Board to receive such recommendations.

If the Board determines to propose a new or amended Professional Auditing Standard, it will do so in accordance with an exposure process. Normally, the Board will publish the proposal and afford interested persons an opportunity to comment, for a period of no less than 21 calendar days.^{6/} Depending on the nature of the proposal, the Board may, in addition to accepting written comment, hold a public hearing, convene a roundtable meeting, commission research, or take other steps to obtain input and data concerning the proposed standard. The Board may also ask the advisory group or a task force to advise it concerning the proposal, and the advisory group or task forces may, in some cases, hold hearings, convene roundtables, or commission research. After considering the public comment (and any other relevant input received), the Board will vote on whether or not to adopt the proposed standard. Approval will require the affirmative vote of a majority of the Board. Any standard adopted by the Board will not take effect unless approved by the Commission in accordance with the Act.^{7/}

^{6/} There may be occasional exceptions to the public comment process, such as in emergencies or other unusual circumstances where further public comment does not appear necessary. The Board will only have a comment period of less than 21 days if it determines that a shorter period is necessary or appropriate under the circumstances. In any such cases, Board rules would still be submitted to the Commission for approval under Section 107 of the Act, which would normally entail a further public comment period.

^{7/} Section 107(a)(4) of the Act generally requires the Commission to publish any proposed rule of the Board for public comment before determining whether to approve the rule or to institute disapproval proceedings.

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C. Advisory Groups and Task Forces

Section 103(a)(4) of the Act provides that the Board shall “convene, or authorize its staff to convene, such expert advisory groups as may be appropriate . . . to make recommendations concerning the content (including proposed drafts) of auditing, quality control, ethics, independence, or other standards required to be established under this section.” The Board has decided to exercise this authority to convene a standing advisory group to participate in the standards-setting process. The role of the advisory group will be to assist the Board in reviewing existing auditing standards, in formulating new or amended standards, and in evaluating proposed standards suggested by other persons. The Board contemplates that the advisory group will have somewhere between 15 and 30 members. The Board may, based on the circumstances of particular projects, form ad hoc task forces comprised of smaller groups of members of the advisory group, of the Board’s staff, and possibly other persons.

The advisory group will be comprised of individuals with a variety of perspectives, including practicing auditors, preparers of financial statements, the investor community, and others.^{8/} The Board expects that the advisory group will have fairly equal representation among these broad groups and that no one group will dominate the advisory group.^{9/} The members will be selected by the Board, although the Board will consider nominations for advisory group members from a broad range of persons with an interest in the quality of the audits of public companies. Each member of the advisory group will have expertise in at least one of the following areas:

- Public company accounting;

^{8/} The Board anticipates that academia, state accounting regulators, and similar interest-groups will be represented on the advisory group.

^{9/} For example, given the broad range of constituencies the Board intends to invite, the Board expects that each of the accounting/auditing, finance, and investment fields will generally be limited to no more than one-third of the total group

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- Public company auditing;
- Public company finance;
- Public company governance;
- Investing in public companies; and
- Other disciplines that the Board deems to be relevant.

Members on an advisory group will serve in their individual capacities and therefore may not delegate their duties as advisory group members, including attendance at meetings. Advisory group members will also be subject to certain provisions of the Board's Ethics Code, including provisions designed to protect non-public information and avoid conflicts of interest.^{10/}

D. Board Professional Auditing Standards Agenda

The Board will be vigilant for the need to adopt new Professional Auditing Standards, especially in response to emerging issues and problems that arise in connection with audits of issuers. In addition, there are three standards-setting projects that the Board intends to commence as rapidly as possible following the Commission's determination pursuant to Section 101(d), that the Board is capable of carrying out its responsibilities under the Act. These three projects are described briefly below.

1. Review of Interim Professional Auditing Standards

In Release No. 2003-006, the Board announced that, pursuant to Section 103(a)(3)(B) of the Act, it has adopted certain standards as Interim Professional

^{10/} In a separate release issued today, the Board has invited comment on its proposed Ethics Code. See Proposal of Ethics Code for Board Members, Staff and Designated Contractors and Consultants, PCAOB Rel. No. 2003-004 (April 16, 2003).

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Auditing Standards. These standards were promulgated by various other bodies and pre-date the Commission's determination, under Section 101(d), that the Board is capable of carrying out its responsibilities under the Act. Rules 3200T, 3300T, 3400T, 3500T, and 3600T (which are discussed in Release No. 2003-006) incorporate these Interim Professional Auditing Standards into the Board's rules.

Despite the need to adopt these existing standards on an initial, transitional basis in order to assure continuity and certainty in the standards that govern audits of public companies, the Board has not determined whether it would be appropriate to include any of the Interim Professional Auditing Standards as permanent Board standards.^{11/} In order to make that determination, the Board will establish a schedule for the review of all Interim Professional Auditing Standards. The Board intends to commence this review as soon as possible. The objective of the review will be to determine, on a standard-by-standard basis, whether the Interim Professional Auditing Standards should become permanent standards of the Board, be repealed, or be modified. As the review of each interim standard is completed, the Board will adopt that standard as a permanent Professional Auditing Standard, with or without modifications, repeal the standard, or take any other appropriate action regarding the standard.

The schedule and procedure for the review of the interim standards will be the subject of a separate release. The Board invites public comment and suggestions concerning the appropriate priorities for the review of the Interim Professional Auditing Standards and concerning any changes to them that the Board should consider.

2. Statutory Professional Auditing Standards

A second Board standards-setting project that will commence shortly after the Commission's Section 101(d) determination is the implementation of the provisions of the Act that require the Board to adopt standards in specific areas. For example,

^{11/} The inclusion of the letter "T" after these rules signifies that the rules are only transitional standards.

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Sections 103(a)(2)(A)(i) and (ii) of the Act^{12/} require that the Board adopt auditing standards requiring that registered public accounting firms –

- prepare, and maintain for a period of not less than seven years, audit work papers, and other information related to any audit report, in sufficient detail to support the conclusions reached in such report; and
- provide a concurring or second partner review and approval of such audit report (and other related information), and concurring approval in its issuance, by a qualified person associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer.

Section 103(a)(2)(B) of the Act requires that the Board adopt quality control standards for registered public accounting firms relating to –

- monitoring of professional ethics and independence from issuers on behalf of which the firm issues audit reports;
- consultation within such firm on accounting and auditing questions;
- supervision of audit work;
- hiring, professional development, and advancement of personnel;
- the acceptance and continuation of engagements; and
- internal inspection.

The Board's staff will develop proposals to implement these statutory mandates as quickly as possible. As in the case of the review of the Interim Professional Auditing

^{12/} With respect to standards required by Section 103(a)(2)(A)(iii), see section D.3 of this release, *infra*.

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Standards, the Board may also, where appropriate, seek the assistance of the Board advisory groups and Board task forces.

3. Review of Internal Controls and Section 404 Attestation Standard

In addition to the matters listed above, Section 103(a)(2)(A)(iii) of the Act also requires the Board to adopt auditing standards that require registered public accounting firms to –

“describe in each audit report the scope of the auditor's testing of the internal control structure and procedures of the issuer, required by section 404(b), and present (in such report or in a separate report) –

- (I) the findings of the auditor from such testing;
- (II) an evaluation of whether such internal control structure and procedures –
 - (aa) include maintenance or records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer;
 - (bb) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and
- (III) a description, at a minimum, of material weaknesses in such internal controls, and of any material noncompliance found on the basis of such testing.”

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This requirement complements Section 404 of the Act. Section 404(a) requires issuers to file with the Commission an annual report assessing the company's internal controls. Section 404(b) provides that the issuer's auditor must "attest to, and report on, the assessment made by the management of the issuer." Section 404(b) further provides that "[a]n attestation made under this subsection shall be made in accordance with standards for attestation engagements issued or adopted by the Board."

The Commission has proposed rules to implement the internal control reporting provisions of Section 404.^{13/} The Board recognizes its correlative obligation to issue or adopt standards for the attestation of these reports by issuers' auditors. In this connection, the Board is aware that the Interim Professional Auditing Standards include a pre-existing standard governing engagements to issue an examination report on the effectiveness of an entity's internal control over financial reporting (or on an assertion thereon).^{14/} The Board is also aware that, on March 18, 2003, the Auditing Standards Board of the American Institute of Certified Public Accountants issued an exposure draft of an additional standard on internal control reporting.^{15/} In discharging its responsibilities under Sections 103(a)(2)(A)(iii) and 404(b), the Board will review both the existing standard and the AICPA's proposal.

The Board intends to address this issue as a matter of priority. To that end, the Board intends to convene a roundtable meeting in the near future to explore whether a new standard with respect to internal control reporting is needed in light of Section

^{13/} See SEC, Proposed Rule: Disclosure Required by Sections 404, 406 and 407 of the Sarbanes-Oxley Act of 2002, Rel. No. 33-8138 (October 22, 2002).

^{14/} See Reporting on an Entity's Internal Control Over Financial Reporting, ASB Statement on Standards for Attestation Engagements No. 10 (Codification of Statements on Auditing Standards, AT sec. 501 (AICPA 2002)).

^{15/} See Proposed Statements on Auditing Standards, Auditing an Entity's Internal Control Over Financial Reporting in Conjunction With the Financial Statement Audit, AICPA ASB (March 18, 2003).

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404(b). The details of the Roundtable meeting will be the subject of a separate release. If the Board determines that such a standard is needed, it will commence a rulemaking proceeding, in accordance with the general procedures outlined in this release, to determine the nature and content of that standard. Interested persons will also be afforded an appropriate opportunity to express their views to the Board in that proceeding.

E. Board Determination Regarding Section 103(a)(3)(A) of the Act

Section 103(a)(3)(A)(i) of the Act authorizes the Board, in discharging its responsibilities with respect to professional standards, to “adopt as its rules, subject to the terms of section 107, any portion of any statement of auditing standards or other professional auditing standards” that were proposed by a professional group of accountants designated or recognized by the Board, by rule, for that purpose, or by an advisory group convened by the Board. Even if the Board elected to designate such a group, the Board would still be required to determine that any standard proposed by the designee meets the requirements of the Act. In addition, the Board may modify, supplement, revise, or subsequently amend, modify, or repeal, in whole or in part, any portion of any such standard.

The Board has decided not to exercise its authority under Section 103(a)(3)(A) to designate a group of accountants or an advisory group as a source of auditing standards. Absent future Board action, no Board advisory group or outside group will have any special ability to submit proposed standards to the Board.^{16/} Nevertheless, as

^{16/} Under Section 103(a)(3)(A) of the Act, the effect of an advisory group or a professional group of accountants being designated, by rule, by the Board for standards-setting purposes appears to be that the Board would then engage in standards-setting by adopting (with any necessary modifications, supplements or revisions) the advisory or professional group’s standards without engaging in its own rulemaking processes. See Report of the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, on S. 2673, S. Rep. No. 107-205 (July 26, 2002) (“The Board may adopt as part of its rules (and modify as appropriate for that purpose, at the time of

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discussed above, the Board will consider carefully proposed auditing standards recommended to it by any person or group, including any group of accountants. If the Board determines that it is appropriate and consistent with the Board's standards-setting priorities and statutory responsibilities, it will publish such proposals for comment or take other appropriate action.

The Board will continue to consider its authority under Section 103(a)(3)(A) and could, in the future, designate one or more advisory groups or professional groups of accountants pursuant thereto. Any such designation would, pursuant to the requirements of Section 103(a)(3)(A), be made by a rule of the Board, subject to the Board's public rulemaking procedures, including Commission approval.

F. Request For Public Comment

The Board invites the views of interested persons with respect to the issues raised for comment in this release. Written comments should be sent to Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments may also be submitted by e-mail to comments@pcaobus.org or through the Board's website at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 004 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on May 12, 2003.

Following the close of the comment period, the Board will determine whether to adopt, and submit to the Commission for approval, proposed Rule 3100 (and the related definition) and Rule 3700.

adoption or thereafter), any portion of a statement of auditing, quality control, or ethics standards that meets the bill's statutory tests and that is proposed (i) by a professional group of accountants (designated by a rule of the Board for that purpose), or (ii) by one or more advisory groups of practicing accountants or other interested parties convened by the Board.”).



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On the 16th day of April, in the year 2003, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ISSUED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
Acting Secretary

April 16, 2003

APPENDICES:

1. Proposed Rules Relating to Professional Auditing Standards and Advisory Groups
2. Section-by-Section Analysis of Proposed Rules Relating to Professional Auditing Standards and Advisory Groups

**Appendix 1 – Proposed Rules Relating to
Professional Auditing Standards and Advisory Groups**

RULES OF THE BOARD

SECTION 1. GENERAL PROVISIONS

1001. Definitions of Terms Employed in Rules.

When used in the Rules, unless the context otherwise requires:

(p)(iv) Professional Auditing Standard

The term “professional auditing standard” means any auditing standard, standard for attestation engagements, quality control policy or procedure, ethical or competency standard, and independence standard (including any rule implementing title II of the Act) that is established or adopted by the Board under Section 103 of the Act.

SECTION 7. PROFESSIONAL STANDARDS

Part 1 – General Requirements

3100. Professional Auditing Standards Applicable to Registered Public Accounting Firms.

A registered public accounting firm and its associated persons shall comply with all applicable professional auditing standards.

Note: Under Section 102(a) of the Act, public accounting firms are not required to register with the Board until 180 days after the date of the determination of the Commission under section 101(d) that the Board has the capacity to carry out the requirements of Title I of the Act (the “mandatory registration date”). The Board intends that, during the period preceding the mandatory registration date, this rule would apply to public accounting firms that would be required to be registered after the mandatory registration date and to associated persons of those firms, as if those firms were registered public accounting firms.

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Part 7 – Establishment of Professional Standards

3700. Advisory Groups.

(a) Formation.

To assist it in carrying out its responsibility to establish professional auditing standards, the Board will convene one or more advisory groups, in accordance with Section 103(a)(4) of the Act.

(b) Composition.

Advisory groups, in combination or as sub-groups within one advisory group, will contain individuals with expertise in the following areas:

- (1) Public company accounting;
- (2) Public company auditing;
- (3) Public company finance;
- (4) Public company governance;
- (5) Investing in public companies; and
- (6) Other areas that the Board deems to be relevant to one or more standard.

(c) Selection of Members of Advisory Groups.

Members of advisory groups will be selected by the Board, in its sole discretion, based upon recommendations provided by:

- (1) Board members;
- (2) Staff of the Board;

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- (3) The Commission or its staff;
- (4) Professional groups of accountants;
- (5) Registered public accounting firms;
- (6) Investors;
- (7) Institutions of higher learning; or
- (8) Any other person or body that the Board deems to have an interest in the accuracy of public company financial statements.

(d) Personal Membership.

Membership on an advisory group will be personal to the individuals selected to serve on the advisory group. A member's functions and responsibilities, including attendance at meetings, may not be delegated to others.

(e) Ethical Duties of Advisory Group Members.

Members of an advisory group shall comply with EC 3, EC 8(a) and EC 9 of the Board's Ethics Code.

(f) Ad Hoc Task Forces.

The Board may, in its discretion, establish ad hoc task forces. The membership of such task forces may include, but is not limited to, advisory group members.

Appendix 2 – Section-by-Section Analysis of Proposed Rules Relating to Professional Auditing Standards and Advisory Groups

Rules Relating to Professional Auditing Standards

The proposed rules relating to professional auditing standards consist of PCAOB Rule 3100, plus a new definition that would appear in Rule 1001. Each of the proposed rules, and the new definition, is discussed below.

Rule 1001 – Definitions of Terms Employed in Rules

Rule 1001 contains definitions of terms used in the Board's rules.

Professional Auditing Standards

Rule 1001(p)(iv) would define “professional auditing standard” as any auditing standard, standard for attestation engagements, quality control policy or procedure, ethical or competency standard, and independence standard (including any rule implementing title II of the Act) established or adopted by the Board under Section 103 of the Act. Although the term includes standards other than auditing standards, the Board has used the term “professional auditing standards,” rather than “professional standards,” because the term “professional standards” is defined otherwise in Section 2(a)(10) of the Act. The term “professional auditing standards” is similar to that portion of the definition of the term “professional standards” that appears in Section 2(a)(10)(B) of the Act.

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Rule 3100 – Professional Auditing Standards Applicable to Registered Public Accounting Firms

Rule 3100 would provide that a registered public accounting firm and its associated persons must comply with all applicable professional auditing standards. A note to the rule clarifies that the rule is intended, before the date 180 days after the Commission's determination under Section 101(d) of the Act, to apply to those public accounting firms that will be required to register with the Board in order to continue to participate in the audits of issuers after that date. This rule is intended to codify the obligation of registered public accounting firms and their associated persons to comply with applicable professional auditing standards and to ensure that the Board's professional auditing standards are enforceable.

Rules Relating to Advisory Groups

Rule 3700 – Advisory Groups

Rule 3700 addresses certain basic matters concerning the formation and use of advisory groups in the Board's standards-setting process. The rule provides that the Board will convene one or more advisory groups, as contemplated in Section 103(a)(4) of the Act. Any advisory group will consist of individuals with expertise in certain,

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specified areas relevant to the Board's standards-setting responsibilities. Members of an advisory group will be selected by the Board. The rule would also permit certain private and governmental groups with an interest in the accuracy of public company financial statements to recommend advisory group members to the Board. The rule also would provide for the Board to establish ad hoc task forces. While such task forces may include advisory group members, a task force may also include other persons.

The rule would further provide that membership on an advisory group will be personal to the individuals selected and that the functions of an advisory group member, including attendance at meetings, may not be delegated to others. This provision is based on a comparable provision in the Financial Accounting Standards Board's rules governing the members of the Financial Accounting Standards Advisory Council (FASAC).

Finally, Rule 3700 would provide that members of a Board advisory group must comply with certain provisions in the Board's Ethics Code. Specifically, the Rule would make advisory group members subject to EC 3, EC 8(a) and EC 9 of the Board's proposed Ethics Code. These provisions of the Board's proposed Ethics Code address, respectively, general ethical principles applicable to service for the Board,



Appendix 2 – Section-by-Section Analysis of Proposed Rules
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disqualification in the case of conflicts of interest, and the non-disclosure of non-public information.