THE WORK OF THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

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Public Company Accounting Oversight Board

Mr. Goelzer is a Member of the Public Company Accounting Oversight Board. Phoebe Brown, Special Counsel, assisted in the preparation of this paper. The views expressed herein are solely those of the authors and are not necessarily those of the Public Company Accounting Oversight Board or any of its other members or staff. The date of this outline is August 14, 2003.
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THE WORK OF THE
PUBLIC COMPANY ACCOUNTING OVERSIGHT
BOARD

Daniel L. Goelzer
Board Member

This outline describes the powers and responsibilities of the Public Company Accounting Oversight Board (the "Board" or "PCAOB"). The outline is based on Title I of the Sarbanes-Oxley Act of 2002 ("the Act") (and the legislative history thereof) and on the Board’s rules, as adopted through August 14, 2003.\footnote{Under Section 107 of the Act, the rules of the Board do not take effect until approved by the Securities and Exchange Commission. As of the date of this outline, the Commission has approved the Board’s Bylaws and rules governing funding, registration and interim auditing and other professional standards. See Sections II.A.3, II.C.3, IV.A and V.A.3 of this outline, infra.} Citations to the part of the Act (or its legislative history) from which descriptions of particular provisions have been drawn, and to the Board’s rules and bylaws, appear in brackets. All proposed and final Board rules are available on the Board’s website at www.pcaobus.org.

I. Introduction

The Act establishes the Board to oversee the audit of public companies that are subject to the securities laws, in order to protect the interests of investors and 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. [Section 101(a)]

The Report of the Committee on Banking, Housing, and Urban Affairs of the United States Senate to Accompany S. 2673 (July 3, 2002) ("Senate Committee Report")\(^2\) states:

The bill creates a strong independent board to oversee the conduct of the auditors of public companies * * *. [Senate Committee Report at 2]

The new Board may, subject to review by the Securities and Exchange Commission * * * establish, adopt, or modify auditing, quality control, ethics, and independence standards for public company audits, inspect accounting firms, investigate potential violations of applicable rules relating to audits, and impose sanctions if those violations are established. [Senate Committee Report at 4]

Floor statements by proponents of S. 2673 are similar. For example:

\(^2\) The Act is the result of the reconciliation of the Public Company Account-ing Reform and Investor Protection Act of 2002 (S. 2673), which passed the Senate on July 15, 2003, and the Corporate Auditing and Accountability, Responsibility, and Trans-parency Act of 2002 (H.R. 3763), which passed the House of Representatives on April 24, 2002. Portions of the Corporate Fraud Accountability Act of 2002 (H.R. 5118), which passed the House of Representatives on July 16, 2002, are also included in the Act.
The bill * * * creates a new independent regulator for the accounting profession. The new body will act as a strong, independent, full-time board with significant authority to regulate auditors of public companies. The independent board will have clear authority for setting auditor standards and important investigative standards. It strengthens audit reporting standards for the accounting profession * * *. Remarks of Senator Dodd. [Congressional Record at S6773 (July 15, 2002)]

II. Establishment and Administrative Provisions: Organization, Membership, Funding and Start-Up of the Board

A. Establishment and Organization of the Board

The Board is a body corporate, and operates as a nonprofit corporation. The Board has succession until dissolved by an Act of Congress. [Section 101(a)]

1. Nongovernmental Status

The Board is not an agency or establishment of the United States Government, and, except as otherwise provided in the Act, is subject to, and has all the powers conferred upon, a nonprofit corporation by the District of Columbia Nonprofit Corporation Act. No member, employee, or agent of the Board is an officer, employee, or agent of the Federal Government by reason of such service. [Section 101(b)]
2. **Corporate Powers**

The Board, subject to the oversight of the Securities and Exchange Commission ("Commission"), has the following corporate powers [Section 101(f)(1)-(6)] --

- to sue and be sued, complain and defend, in its corporate name and through its own counsel, with the approval of the Commission, in any Federal, State, or other court;

- to conduct its operations and maintain offices, and to exercise all other rights and powers authorized by the Act, in any State, without regard to any qualification, licensing, or other provision of law in effect in such State (or a political subdivision thereof);

- to lease, purchase, accept gifts or donations of or otherwise acquire, improve, use, sell, exchange, or convey, all of or an interest in any property, wherever situated;

- to appoint such employees, accountants, attorneys, and other agents as may be necessary or appropriate, and to determine their qualifications, define their duties, and fix their salaries or other compensation (at a level that is comparable to private sector self-regulatory, accounting, technical, supervisory, or other staff or management positions);

- to allocate, assess, and collect accounting support fees and other fees and charges imposed under the Act; and
• to enter into contracts, execute instruments, incur liabilities, and do any and all other acts and things necessary, appropriate, or incidental to the conduct of its operations and the exercise of its obligations, rights, and powers imposed or granted by the Act.

Regarding the Board's authority to hire staff, the Senate Committee Report states:

It is essential that the Board have a strong, well-trained, and experienced staff, of sufficient size to carry out its responsibilities. A number of witnesses emphasized, for example, that inspections must no longer be left to peer reviews of one accounting firm by another. The bill makes plain, as the Committee intends, that the Board is to provide for staff salaries that are fully competitive with those for comparable private-sector self-regulatory, accounting, technical, supervisory, or related staff or management positions. [Senate Committee Report at 7]

3. Bylaws

On January 9, 2003, the Board, by a unanimous vote, adopted bylaws to govern its operations. On April 25, 2003, the Board amended Article VI of the bylaws to provide for the powers of a Chair/Chief Executive Officer.\(^3\) The

\(^3\) On January 9, when the Bylaws were adopted, the Board was acting without a permanent Chair. In recognition of this fact, the bylaws did not address the division of powers and duties between the Chair and other members of the governing board. On April 15, 2003, the Commission

The bylaws include provisions addressing the following matters, among others --

- the establishment of the Board’s principal office in Washington, D.C.;

- the composition of a “governing board” of the Board, the powers and duties of the governing board, the powers and duties of the Chair/Chief Executive Officer, and the quorum requirements of the governing Board;

- the Board’s regular public meetings and special meetings;

- the powers and duties of officers of the Board;

- indemnification of current and former employees, officers, and members of the Board;

- procedures for amendments to the Board’s bylaws;

- the Board’s fiscal year; and

announced a nominee for Board Chair. Accordingly, on April 25, 2003, the Board amended Article VI of the bylaws to provide for the powers of a Chair/Chief Executive Officer. [PCAOB Amendment No. 1 -- Proposed Bylaws, Form 19b-4]

\[4/\] Bylaws are “rules of the Board,” as defined in Section 2(a)(13) of the Act, and must be approved by the Commission. See Section IX.A of this outline, infra.
• governing board approval of capital expenditures.

B. Membership of the Board

1. Composition; Qualifications of Board Members

The Board has five members. Board members are to be appointed --

from among prominent individuals of integrity and reputation who have a demonstrated commitment to the interests of investors and the public, and an understanding of the responsibilities for and nature of the financial disclosures required of issuers under the securities laws and the obligations of accountants with respect to the preparation and issuance of audit reports with respect to such disclosures. [Section 101(e)(1)]

Two members, and only two members, of the Board must be, or have been, certified public accountants. If one of those two members is the chairperson, he or she may not have been a practicing certified public accountant for at least five years prior to his or her appointment to the Board. [Section 101(e)(2)]

Each member of the Board must serve on a full-time basis, and may not be employed by any other person or engage in any other professional or business activity. No member of the Board may share in profits of, or receive payments from, a public accounting firm, other than fixed payments under standard retirement arrangements. [Section 101(e)(3)]
2. **Appointment of Board Members**

The Commission, after consultation with the Chairman of the Board of Governors of the Federal Reserve System and the Secretary of the Treasury, appoints the chairperson and other members of the Board. A vacancy on the Board does not affect the powers of the Board, but is to be filled in the same manner as initial appointments. [Section 101(e)(4)]

3. **Terms of Board Service**

The term of service of each Board member is five years, and until a successor is appointed. The terms of the initial Board members (other than the chairperson) expire in annual increments, one on each of the first four anniversaries of the initial date of appointment (i.e., October 25, 2002). Any Board member appointed to fill a vacancy occurring before the expiration of the term for which the predecessor was appointed is appointed only for the remainder of that term. No person may serve as a member of the Board, or as chairperson of the Board, for more than two terms, whether or not such terms of service are consecutive. [Section 101(e)(5)] The Commission for good cause may remove a member of the Board. [Section 101(e)(6)]

C. **Board Funding**

The Act establishes a mechanism for the funding, by all publicly traded companies, of the Board and of the accounting standard-setting body designated pursuant to Section 19(b) of the Securities Act of 1933. (The Financial Accounting Standards Board will presumably be the accounting standard-setting body.) Under this mechanism, the budget of the Board, (reduced by any registration or annual fees received from accounting firms during the preceding year) and the budget of the standard-setting body,
are payable from a fee levied against public companies.\footnote{The accounting support fee is payable by “issuers.” Section 2(a)(7) of the Act defines the term “issuer” to mean an issuer (as defined in Section 3 of the Exchange Act), the securities of which are registered under Section 12 of that Act or that is required to file reports under Section 15(d), or that files or has filed a registration statement that has not yet become effective under the Securities Act of 1933.} This fee is referred to as the “annual accounting support fee.” [Section 109(a)]

1. Initial Funding

From the unexpended balances of the Commission appropriation for fiscal year 2003, the Secretary of the Treasury may advance to the Board the amount necessary to cover the expenses of the Board during its first fiscal year. [Section 109(j)] The budget for the first fiscal year of the Board must be prepared and approved promptly following the appointment of the initial five Board members in order that the Board can accomplish the organizational tasks contemplated by the Act. [Section 109(b)] The Board adopted a budget for calendar year 2003 at an open meeting on April 23, 2003 and submitted that budget to the Commission for its approval. The Commission approved the budget on August 1, 2003. [Order Approving Public Company Accounting Oversight Board Budget and Annual Accounting Support Fee for Calendar Year 2003, Exchange Act Release No. 48276 (August 1, 2003)]

2. Annual Board Budget

The Board must establish a budget for each fiscal year. This budget must be reviewed and approved internally...
not less than one month prior to the commencement of each fiscal year (or at the beginning of the Board's first fiscal year, which may be a short fiscal year). The budget is subject to Commission approval. [Section 109(b)]

3. **Annual Accounting Support Fee for the Board**

The Board must establish, with the approval of the Commission, a reasonable annual accounting support fee (or a formula for the computation thereof), to establish and maintain the Board. The annual fee may also cover costs incurred in the Board's first fiscal year, or the Board may recover these costs by a separate levy. [Section 109(d)(1)]

The rules of the Board must provide for the equitable allocation, assessment, and collection by the Board (or an agent appointed by the Board) of the fee established under annual accounting support fee among issuers. The Board's rules may allow for differentiation among classes of issuers, as appropriate. [Section 109(d)(2)] The amount of fees collected for a fiscal year on behalf of the Board may not exceed the recoverable budget expenses of the Board (which may include operating, capital, and accrued items). [Section 109(f)]

On April 18, 2003, the Board issued final rules with respect to the accounting support fee[^6] [PCAOB Release No. 2003-003 (April 18, 2003)] and submitted the rules to the

Commission for approval pursuant to Section 107 of the Act. On July 30, 2003, the Board amended its final rules to provide for an exception to the requirement on auditor confirmation of payment of the accounting support fee, and submitted the amendment to the Commission of its approval. The Commission approved the Board’s funding rules on August 1, 2003.\footnote{\textit{Order Approving Proposed Rules on Funding and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 1 to the Proposed Rules}, Exchange Act Release No. 48278 (August 1, 2003)} Under these rules, the Board will compute the accounting support fee once annually. The accounting support fee will be equal to the Board’s budget for that year, as approved by the Commission, less the amount of registration and annual fees received during the prior year from public accounting firms. [PCAOB Rule 7100] (Accounting firm registration and annual fees must be set at a level that covers the cost of processing and reviewing registration applications and annual reports.)

4. **Allocation of the Accounting Support Fees Among Issuers**

For purposes of allocating the accounting support fee among public companies, the Board’s rules divide issuers into four classes [PCAOB Rule 7101(a)] --

- **Equity Issuers class**: Publicly-traded companies with average monthly equity market capitalization, based on all classes of common stock, greater than $25 million during the prior calendar year;

- **Investment Company Issuers class**: Registered investment companies and other issuers that have elected to be regulated as business development companies with average monthly market capitalization or net asset value greater than $250 million during the prior calendar year;

- **Issuers Permitted Not to File class**: All issuers that have a basis under a Commission rule, or pursuant to other action of the Commission or its staff, not to file audited financial statements with the Commission or to file modified financial statements; and

- **All Other Issuers class**: All issuers that do not fall within one of the other three classes.

Each year, the accounting support fee will be allocated among the issuers in these four classes in the following manner:  

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§/ This allocation is based on Section 109(g) of the Act, which provides that the Board’s budget amount is to be allocated among issuers such that each issuer’s share is equal to the total amount, multiplied by a fraction --

- the numerator of which is the issuer’s average monthly equity market capitalization for the 12-month period immediately preceding the beginning of the fiscal year to which the budget relates; and
• Each company in the Equity Issuer and Investment Company Issuer classes will be allocated an amount equal to the accounting support fee, multiplied by a fraction. The numerator of the fraction will be the issuer’s average, monthly market capitalization during the preceding calendar year. The denominator will be the sum of the average, monthly market capitalizations of all Equity and Investment Company Issuers. For purposes of this allocation, the market capitalization of an investment company issuer will be ten percent of the investment company’s market capitalization or net asset value. [PCAOB Rule 7101(b)(1)]

• All issuers in the other two classes – i.e., the Issuers Permitted Not to File class and the All Other Issuers class – will be allocated a share of zero. [PCAOB Rule 7101(b)(2)]

Each issuer in the Equity Issuer and Investment Company Issuer classes is required to pay its share of the accounting support fee, as determined by the foregoing calculation, rounded to the nearest one hundred dollars. [PCAOB Rule 7102]

5. Notice of Allocation and Assessment and Collection

After the allocation of the accounting support fee is determined, the Board will use its best efforts to send a notice

• the denominator of which is the average monthly equity market capitalization of all issuers for such 12-month period.
of assessment to each issuer to which a share of the fee has been allocated. Issuers will be assessed for their share of the accounting support fee, rounded to the nearest hundred. If an issuer’s share of the accounting support fee is less than $50, that issuer’s share will be rounded to zero. Notices will be sent either electronically or by first-class mail. [PCAOB Rule 7102] PCAOB Rule 7102(c) sets forth a procedure for an issuer to contest the class in which it was placed or the calculation by which its share was determined.

Payment is due on the 30th day after transmittal of the notice. Support fee allocations that are unpaid on that date will accrue interest at the rate of 6 percent per annum. If an issuer has not paid by the 60th day, and the issuer has not filed a petition contesting its allocation, the Board may send a second notice by certified mail. [PCAOB Rule 7103(a)] If the Board has sent a second notice and payment has still not been made by the 90th day, the Board may report the issuer’s non-payment to the Commission. [PCAOB Rule 7103(c)] Further, with certain exceptions, no registered public accounting firm will be permitted to sign an unqualified audit opinion with respect to an issuer’s financial statements, or issue a consent to include an audit opinion issued previously, unless the auditor has ascertained that the issuer has outstanding no past-due share of the accounting support fee. [PCAOB Rule 7103(b)]

6. Issuer Obligation to Pay Accounting Support Fee

Section 13(b)(2) of the Securities Exchange Act of 1934 ("Exchange Act") requires issuers to pay their allocable share of a reasonable annual accounting support fee or fees, determined in accordance with Section 109 of the Act. [Section 109(h)] In this regard, Senator Feinstein stated, on the Senate floor:
Unlike the Public Oversight Board, which depended on fees from the very auditors it was meant to regulate, this new board will be funded by mandatory fees paid by all public companies. These are fees that cannot be withheld at the whim of those who have the greatest interest in undermining the work of the board. [Cong. Rec. at S6762 (July 15, 2002)]

7. Inapplicability of Appropriations Procedures

Neither the Board nor the standard-setting body is subject to the Congressional procedures for the authorization and appropriation of public funds. Both organizations may utilize additional sources of revenue, such as earnings from publication sales, for their activities, provided these additional revenues do not jeopardize, in the judgment of the Commission, actual or perceived independence. [Section 109(i)] Accounting support fees and other receipts of the Board (and of the standard-setting body) are not monies of the United States. [Section 109(c)(1)]

8. Funds Generated From the Collection of Monetary Penalties

Subject to an appropriations act, all funds collected by the Board as a result of the assessment of monetary penalties must be used to fund a merit scholarship program for undergraduate and graduate students enrolled in accredited accounting degree programs. This scholarship program will be administered by the Board or by an entity or agent identified by the Board. [Section 109(c)(2)]

D. Start-up and Commission Determination

Prior to the Board’s appointment, the Commission was responsible for planning the administrative transition to the Board's operation. After their appointment, the Board members were required to take such action (including hiring of staff, proposal of rules, and adoption of initial and transitional auditing and other professional standards) as necessary or appropriate to enable the Commission to determine, not later than 270 days after the date of enactment of the Act, that the Board is so organized and has the capacity to carry out the requirements of the Act, and to enforce compliance with the Act by registered public accounting firms and associated persons thereof. [Section 101(d)]

On April 25, 2003, the Commission determined that the Board had satisfied the requirements of Section 101(d) of the Act. [Order Regarding Section 101(d) of the Sarbanes-Oxley Act of 2002, Securities Act Release No. 8223 (April 25, 2003).] In Release No. 8223, the Commission stated:

Since the appointment of its board members, the PCAOB has undertaken many actions to demonstrate its readiness to carry out the requirements of the Act. For example, it has hired or substantially completed the hiring process to fill, on a permanent or acting basis, a majority of its key positions, including the Director of Registration and Inspections and the Chief Auditor. The PCAOB has adopted by-laws and proposed for public comment a code of conduct and ethical standards for PCAOB members and staff.

The PCAOB has adopted its budget for the calendar year 2003. It also has determined and
submitted to the Commission a proposed formula for the computation of an Annual Accounting Support Fee for calendar year 2003. The PCAOB has adopted, and submitted to the Commission for approval, a plan for assessment, billing and collection of registration fees, annual fees and Annual Accounting Support Fees.

The PCAOB has begun to adopt rules for the profession. For example, it has proposed rules relating to the registration of public accounting firms and has supplemented its comment process on that proposal by holding a public roundtable meeting to solicit views on issues relating to the registration of non-U.S. public accounting firms. The PCAOB has adopted interim professional standards relating to auditing, attestation, independence, quality control, and ethical conduct of auditors. These standards are the subject of a separate Commission Order. After the date of that Order, no professional standards in these areas, as they relate to the audit of public companies, will take effect unless approved by the PCAOB under its statutory rulemaking process and published for comment and approved by the Commission. The PCAOB also has issued a policy statement setting forth a blueprint for its future standard-setting procedures, including a planned review of the interim standards.

Finally, the PCAOB has developed a plan for inspecting accounting firms. It has also prepared a plan to develop procedures and standards governing disciplinary proceedings.
and the imposition of sanctions against accounting firms and their associates.

III. Powers of the Board

A. Regulatory Responsibilities

Subject to the Commission's oversight authority, the Board has the following powers [Section 101(c)(1) through (8)] --

- To register public accounting firms that prepare audit reports for issuers;

- To establish or adopt, or both, by rule, auditing, quality control, ethics, independence, and other standards relating to the preparation of audit reports for issuers;

- To conduct inspections of registered public accounting firms;

- To conduct investigations and disciplinary proceedings concerning, and impose appropriate sanctions where justified upon, registered public accounting firms and associated persons of such firms;

- To perform such other duties or functions as the Board (or the Commission, by rule or order) determines are necessary or appropriate to promote high professional standards among, and improve the quality of audit services offered by, registered public accounting firms and associated persons thereof, or otherwise to carry out the Act,
in order to protect investors, or to further the public interest;

- To enforce compliance by registered public accounting firms and their associated persons with the Act, the Board's rules, professional standards, and the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants; and

- To set the budget and manage the operations of the Board and the staff of the Board.

B. Rulemaking

The term "rules of the Board" means the bylaws and rules of the Board (as submitted to, and approved, modified, or amended by the Commission), and those stated policies, practices, and interpretations of the Board that the Commission, by rule, may deem to be rules of the Board, as necessary or appropriate in the public interest or for the protection of investors. [Section 2(a)(13)] Subject to the Commission's oversight, the Board has the authority to adopt rules [Sections 101(g)(1) through (4)] --

- To provide for the operation and administration of the Board, the exercise of its authority, and the performance of its responsibilities under the Act;

- To permit, as the Board determines necessary or appropriate, delegation by the Board of any of its functions to an individual member or employee of the Board, or to a division of the Board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any matter (subject to certain procedural limitations);
• To establish ethics rules and conduct standards for Board members and staff, including a bar on practice before the Board (and the Commission, with respect to Board matters) of one year for former members of the Board, and appropriate periods (not to exceed one year) for former Board staff; 9/ and

• To provide as otherwise required by the Act.

IV. Registration of Accounting Firms

A. Mandatory Registration

Beginning 180 days after the date of the determination of the Commission that the Board has the capacity to carry out its responsibilities under the Act, it will be unlawful for any person that is not a registered public accounting firm to prepare or issue, or to participate in the preparation or issuance of, any audit report with respect to any issuer. [Section 102(a)] Since the Commission issued this determination on April 25, 2003, (see Section II.D of this outline, supra), the statutory registration deadline is October 22, 2003. 10/

9/ On April 18, 2003, the Board adopted an ethics code to implement provisions of Section 101(g)(3) of the Act and submitted the code to the Commission for approval pursuant to Section 107 of the Act. The ethics code governs the conduct of the members, employees, and certain contractors and consultants of the Board. [PCAOB Release No. 2003-008]

10/ In the case of foreign accounting firms, the Board has extended the registration deadline to April 19, 2004. See Section VIII.D.3 of this outline, infra.
On May 6, 2003, the Board issued final rules to implement Section 102 of the Act.\textsuperscript{11/} [PCAOB Release No. 2003-007 (May 6, 2003)] These rules were submitted to the Commission for approval pursuant to Section 107 of the Act on May 8, 2003 and were approved by the Commission on July 16, 2003. [Order Approving Proposed Rules Relating to Registration System, Exchange Act Release No. 48180 (July 16, 2003).] In Release No. 48180, the Commission stated:

Title I of the Act assigns the Board the formidable task of designing and implementing a registration and oversight system within a relatively short period of time. The investor protection goals of the Act justify the need for prompt action, but the importance of the Board's task and its potential impact on the public securities markets demand that it be undertaken in a thoughtful and reasoned manner. After careful review of the Board's proposed registration system, the Commission finds that it is consistent with the requirements of the Act and the securities laws and is necessary and appropriate in the public interest and for the protection of investors.

Under these rules, each public accounting firm that prepares or issues any audit report with respect to any issuer

must register with the Board. In addition, any public accounting firm that “plays a substantial role in the preparation and furnishing of an audit report” (as defined in the Board’s rules) must register. [PCAOB Rule 2100]

B. Applications for Registration

1. Form of application

A public accounting firm must use such form as the Board may prescribe, by rule, to apply for registration. [Section 102(b)(1)] Each public accounting firm must submit, as part of its application for registration, the following information, in such detail as the Board specifies [Section 102(b)(2)] --

- the names of all issuers for which the firm prepared or issued audit reports during the immediately preceding calendar year, and for which the firm expects to prepare or issue audit reports during the current calendar year;

- the annual fees received by the firm from each such issuer for audit services, other accounting services, and non-audit services, respectively;

- such other current financial information for the most recently completed fiscal year of the firm as the Board may reasonably request;

- a statement of the quality control policies of the firm for its accounting and auditing practices;

- a list of all accountants associated with the firm who participate in or contribute to the preparation of audit reports, stating the license or certification
number of each such person, as well as the State license numbers of the firm itself;

- information relating to criminal, civil, or administrative actions or disciplinary proceedings pending against the firm or any associated person of the firm in connection with any audit report;

- copies of any periodic or annual disclosure filed by an issuer with the Commission during the immediately preceding calendar year which discloses accounting disagreements between such issuer and the firm in connection with an audit report furnished or prepared by the firm for such issuer; and

- such other information as the rules of the Board or the Commission specify as necessary or appropriate in the public interest or for the protection of investors.

The Board’s rules provide that a public accounting firm must apply for registration with the Board on PCAOB Form 1.\(^{12}\) The application must be filed electronically with the Board through the Board’s web-based system. [PCAOB Rule 2101] Form 1 consists of nine parts, subdivided into 22 items, requiring the disclosure of particular information concerning the applicant and its associated accountants and the applicant’s issuer clients. The information these items call for is, in general, that required by Section 102(b)(2) of the Act. [PCAOB Release No. 2003-007, Appendix 2 – Form 1]

\(^{12}\) Form 1 can be accessed through the Board’s website at [www.pcaobus.org](http://www.pcaobus.org).
2. Consents

In addition to the required information, each application for registration must also include [Section 102(b)(2)] --

- a consent executed by the public accounting firm to cooperate in and comply with any request for testimony or the production of documents made by the Board in the furtherance of its authority and responsibilities (and an agreement to secure and enforce similar consents from each of the associated persons of the public accounting firm as a condition of their continued employment by or other association with such firm); and

- a statement that such firm understands and agrees that cooperation and compliance, as described in the consent, and the securing and enforcement of such consents from its associated persons, in accordance with the rules of the Board, will be a condition to the continuing effectiveness of the registration of the firm with the Board.

Part VIII of Form 1 implements Section 102(b)(2) of the Act and requires such consents to be submitted as an exhibit to Form 1. [PCAOB Release No. 2003-007, Appendix 2 – Form 1, Part VIII]

C. Action on Applications

In order to approve an application, the Board must determine that registration of the applicant 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. [PCAOB Rule 2106(a)] The Board must approve a completed application for registration no later than 45 days after the date of receipt of the application, unless the Board issues a written notice of disapproval to, or requests more information from, the prospective registrant. A written notice of disapproval of a completed application for registration constitutes disciplinary sanction for purposes of the sections of the Act governing Commission review of such sanctions. [Section 102(c)]

Within 45 days of receipt of a completed registration application, the Board must (1) approve the application, (2) issue a written hearing notice, or (3) request more information from the prospective registrant. [PCAOB Rule 2106(b)] A hearing notice must specify the proposed grounds for disapproval and may, at the applicant’s election, be treated as a notice of disapproval, appealable to the Commission. [PCAOB Rule 2106(b)] An applicant that does not elect to treat a hearing notice as a final disapproval waives the requirement that applications must be acted upon in 45 days.

PCAOB Release No. 2003-007 states that, in the event that a hearing is held on an application for registration, the staff of the Board's Division of Registration and Inspections will be required to present evidence supporting the proposed grounds for disapproval of registration. The applicant will have the opportunity to present contrary evidence and to demonstrate why, in its view, the application should be granted. At the close of the hearing, the presiding officer will issue a written decision concerning whether the application should be granted or disapproved and setting forth the findings and conclusions on which that decision is based. The decision of the hearing officer will constitute the Board's action on the application, except that hearing officer decisions will be reviewable by the Board, at the request of either party. If the hearing officer disapproves an
application, and if the Board does not review the decision of
the hearing officer, that decision will constitute the Board's
written notice of disapproval for purposes of Section
102(c)(2). If the Board reviews the decision of the hearing
officer, the Board will, upon the completion of its review,
issue a further written decision concerning the application.

On July 28, 2003, the Board proposed rules relating
to investigations and adjudications, including rules on
hearings on registration applications. In the event that an
applicant requests such a hearing, the proposed rules provide
that the proceeding would be governed by the procedures
described in Part II and IV of Section 5 of the Board's rules.
[PCAOB Proposed Rules 5500 and 5501] See Section VII of
this outline, infra.

D. Withdrawal from Registration

On July 28, 2003, the Board proposed rules on
procedures by which a firm, once registered, may seek to
withdraw from registration. 13/ [PCAOB Release No. 2003-
014 (July 28, 2003)] Under the proposed rule, a registered
firm may seek to withdraw its registration by filing a request
with the Board on PCAOB Form 1-WD. The firm that files a
Form 1-WD may not, unless it first withdraws its Form 1-
WD filing, engage in the preparation or issuance of, or play a
substantial role in the preparation or furnishing of, an audit
report for an issuer. The proposed rule automatically delays
a firm withdrawal in certain circumstances and, in other
circumstances, allows the Board the flexibility to delay for up
to two years. [Proposed PCAOB Rule 2107]

13/ PCAOB Rulemaking Docket No. 007. The
comment period on the proposed withdrawal from
registration rules closes on August 18, 2003.
E. Periodic Reports

Each registered public accounting firm must submit an annual report to the Board, and may be required to report more frequently, as necessary to update the information contained in its application for registration under this section, and to provide to the Board such additional information as the Board or the Commission may specify. [Section 102(d)]

F. Public Availability

Section 102(e) of the Act requires that registration applications and annual reports of registered public accounting firms (or such portions of such applications or reports as may be designated under rules of the Board) must be made available for public inspection. However, Section 102(e) also states that public availability of registration applications is subject to "applicable laws relating to the confidentiality of proprietary, personal, or other information" and directs the Board to "protect from public disclosure information reasonably identified by the subject accounting firm as proprietary information."\(^{13}\) PCAOB Rule 2300 implements these requirements.

Rule 2300(a) provides that applications for registration will be made public as soon as practicable after the Board approves or disapproves an application. the subject accounting firm as proprietary information." An applicant for registration may request confidential treatment

\(^{14}\) The Board is not an agency or establishment of the United States. See Section 101(a). Therefore, the Privacy Act, 5 U.S.C. § 552a, the Trade Secrets Act, 18 U.S.C. § 1905, and similar laws that restrict disclosure by federal departments and agencies of personal or proprietary information are not applicable to the Board.
of any portion of an application that has not been publicly disclosed, and either (i) contains information reasonably identified by the applicant as proprietary, or (ii) is protected from public disclosure by applicable laws related to the confidentiality of proprietary, personal, or other information. [Rule 2300(b)] Confidential treatment requests must contain a detailed explanation of the reasons that, based on the facts and circumstances of the request, the information for which confidentiality is sought meets one of these requirements. [Rule 2300(c)] Pending a determination as to whether to grant the request for confidential treatment, the information in question will not be made available to the public. [Rule 2300(d)] The Board will decide whether to grant confidential treatment requests on a case-by-case basis. If the Board determines to deny a confidential treatment request, the applicant requesting the confidential treatment will be notified in writing of the Board's decision, and of the date on which the information in question will be made public, a reasonable time in advance of such date. [Rule 2300(e)]

V. Auditing Standards

A. Auditing, Quality Control, and Ethics Standards

1. Board Authority With Respect to Auditing Standards

The Act directs the Board to establish (including, to the extent it determines appropriate, through adoption of standards proposed by designated professional groups of accountants or Board advisory groups), and to amend or otherwise modify or alter, such auditing and related attestation standards, such quality control standards, and such 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. [Section 103(a)(1)]

The Senate Committee report elaborates on how the Board is to exercise its standard-setting authority:

The Board’s standard-setting authority, however, is neither intended nor structured to exclude practicing accountants from participation in the standard-setting process. The Board may adopt as part of its rules (and modify as appropriate for that purpose, at the time of 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 parties convened by the Board. [Senate Committee Report at 8]

On April 18, 2003, the Board announced the general process by which it will establish auditing and other professional standards for registered public accounting firms and proposed a rule requiring registered public accounting firms and associated persons to adhere to the Board’s professional standards. [Proposed PCAOB Rule 3100]15/ On June 30, 2003, the Board adopted the rule requiring registered public accounting firms and associated persons to adhere to the Board’s professional standards and a rule on the

establishment of advisory groups and ad hoc task forces. [PCAOB Rules 3100 and 3700][16] These rules were submitted to the Commission for approval pursuant to Section 107 on July 11, 2003. Concerning the standard-setting process, PCAOB Release No. 2003-009 makes the following points --

- Consistent with Section 103(a) of the Act, new professional standards will be established – and existing standards changed – only by Board rulemaking.

- The development of standards should be an open public process in which investors, the accounting profession, the preparers of financial statements, and others have the opportunity to participate. The Board encourages proposals and recommendations concerning professional standards.

- The Board will appoint an advisory group to assist it in standard setting. The advisory group may be divided into subgroups by the Board if the need for special advice arises.

Further, PCAOB Release No. 2003-005 makes the following additional points:

- Proposals for new standards may arise from three sources: (i) The Board, with the advice of its staff, may propose a new standard or a change to an existing standard; (ii) The Board’s advisory group or a Board-appointed task force, may

recommend to the Board that it propose a new standard or a change to an existing standard: (iii) Any other person or group may petition the Board and request that it propose a new standard or a change to an existing standard.

- If the Board determines to propose a new or amended 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. 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 its advisory group or a task force to advise it concerning the proposal, and the advisory group or task forces may hold hearings, convene roundtables, or commission research.

- 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. The Board will, however, consider proposed auditing standards recommended to it by any person or group, including any group of accountants.

2. **Required Auditing and Quality Control Standards**

The Board must include in the auditing standards that it adopts, requirements that each registered public accounting firm [Section 103(a)(2)(A)] --
• 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;

• 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; and

• describe in each audit report the scope of the auditor's testing of the internal control structure and procedures of the issuer and present in a report (i) the findings of the auditor from such testing; (ii) an evaluation of whether such internal control structure and procedures meet certain, specified objectives; 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.

The Board must include in the quality control standards that it adopts with respect to the issuance of audit reports, requirements for every registered public accounting firm relating to [Section 103(a)(2)(B)] --

• 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;

• internal inspection; and

• such other requirements as the Board may prescribe.

PCAOB Release No. 2003-005 discusses these statutory standard-setting projects and indicates that the Board will, as a matter of priority, establish such standards.

3. Authority to Adopt Permanent or Interim Standards Proposed By Other Bodies

In carrying out its responsibilities with respect to auditing standards, the Board may adopt as its rules any portion of any statement of auditing standards or other professional standards that the Board determines satisfy the requirements of the Act that were proposed by a professional group of accountants designated or recognized by the Board for that purpose, or by an advisory group convened by the Board. [Section 103(a)(3)(A)(ii)] Notwithstanding its authority to adopt statements of audit standards proposed by such groups, the Board may modify, supplement, revise, or subsequently amend, modify, or repeal, in whole or in part, any portion of any such statement. [Section 103(a)(3)(A)(ii)] The Board may also adopt standards proposed by such groups as initial or transitional standards, to the extent the Board determines necessary, prior to the Commission determination that the Board is capable of carrying out its responsibilities under the Act. These initial or interim standards must be separately approved (or, presumably,
disapproved) by the Commission at the time of that determination, without regard to the procedures otherwise applicable to the review and approval of Board rules. [Section 103(a)(3)(B)]

On April 18, 2003, the Board adopted certain interim auditing, attestation, quality control, ethics, and independence standards ("Interim Professional Auditing Standards") to be used by registered public accounting firms in the preparation and issuance of audit reports. [PCAOB Release No. 2003-006] In essence, the effect of Release No. 2003-006 is to adopt, as interim Board standards, the auditing, quality control, and ethics standards to which public accounting firms were subject in connection with audits of SEC registrants prior to the creation of the Board. The Board stated that it had taken this action "in order to assure continuity and certainty in the standards that govern audits of public companies." PCAOB Rules 3200T, 3300T, 3400T, 3500T, and 3600T, which were also adopted by the Board in Release No. 2003-006, require registered public accounting firms to follow these interim standards. Since the Board has not determined that any of these standards should be permanently adopted, and the letter "T" has been appended to the rules implementing the transitional standards to emphasize the fact that the standards are temporary.

The Board also announced in Release No. 2003-006 that it plans to review all of the interim professional standards and to determine whether each of the interim standards should be modified, repealed, or made permanent. [PCAOB Release No. 2003-006 (April 18, 2003)] In this regard, the Board stated:

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. In order to make that determination, the Board will establish a schedule and procedure for the review of all Interim Professional Auditing Standards. The objective of that review will be to determine, on a standard-by-standard basis, whether the Interim Professional Auditing Standards should become permanent standards of the Board, should be repealed, or should 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, will repeal the standard, or will take any other appropriate action regarding the standard. (footnote omitted)

Consistent with Section 103(a)(3)(B) of the Act, the Board’s Interim Professional Auditing Standards were approved by the Commission on April 25, 2003.17/ In approving the interim standards, the Commission stated:

Each of the interim standards * * * [adopted by the PCAOB] would remain in effect until modified or superseded, either by PCAOB action approved by the Commission as provided in the Act, or by Commission action pursuant to its independent authority under the

federal securities laws and the rules and regulations thereunder. The Commission finds that the adoption of interim professional standards is consistent with the requirements of the Act and the federal securities laws and is necessary or appropriate in the public interest or for the protection of investors. Accordingly, it is ordered that PCAOB Rules 3200T through 3600T, setting forth interim professional standards for use in connection with the audits of public companies, are hereby approved.

4. Advisory Groups

The Board may convene such expert advisory groups as may be appropriate. The members of these groups may include practicing accountants and other experts, as well as representatives of other interested groups. Membership in such groups is subject to such rules as the Board may prescribe to prevent conflicts of interest. The purpose of these groups is to make recommendations concerning the content (including proposed drafts) of auditing, quality control, ethics, independence, or other standards required under the Act.

As noted above, on June 30, 2003, the Board adopted a rule governing the appointment of such an advisory group.\textsuperscript{18} [PCAOB Rule 3700] In Release No. 2003-009, which adopts this rule, the Board describes the role of the

\textsuperscript{18} PCAOB Rulemaking Docket No. 004. On April 18, 2003, the Board proposed a rule governing the appointment of an advisory group and solicited public comment on its proposal. [PCAOB Release No. 2003-005] The comment period ended on May 12, 2003.
advisory group as assisting the Board in reviewing existing auditing standards, in evaluating proposed standards suggested by other persons, and recommending to the Board new or amended auditing standards. The Board contemplates that the advisory group will initially have approximately 25 members. The Board may, based on the circumstances of particular projects, form ad hoc task forces comprised of specially qualified persons selected by the Board to assist with specific projects. Members of the task force may or may not be members of the advisory group.

Release No. 2003-009 states that the advisory group will be comprised of individuals with a variety of backgrounds, including practicing auditors, preparers of financial statements, investors (both individual and institutional), and others. In order to achieve this diversity, the Board expects that no one field of expertise will predominate among the advisory membership. In determining appointments, the Board intends to solicit nominations, including self-nominations. In evaluating nominations, the Board will seek individuals with an interest in the quality of the audits of public company, among other things.

B. Independence Standards and Rules

The Board is empowered to adopt such rules as may be necessary or appropriate in the public interest or for the protection of investors, to implement Title II of the Act. [Section 103(b)] Title II, which is codified in Section 10A of the Exchange Act, relates to the independence of public company auditors. Title II includes prohibitions against an issuer’s auditor providing any of eight categories of non-audit services to the issuer and requires that the issuer’s audit committee approve in advance the provision of non-audit services that are not prohibited.
Title II also confers on the Board authority --

- To prohibit (in addition to the eight statutory categories of prohibited non-audit services) “any other service that the Board determines, by regulation, is impermissible.” [Section 201(a) (codified in Section 10A(g) of the Exchange Act)]

- To exempt, on a case-by-case basis, any person, issuer, public accounting firm, or transaction from the prohibition against the provision of certain services under Section 10A(g) to the extent that such exemption is necessary or appropriate in the public interest or for the protection of investors. Any exemption granted by the Board is subject to Commission review in the same manner as are Board rules. [Section 201(b) (codified in Section 10A(b) of the Exchange Act)]

C. Cooperation With Designated Professional Groups of Accountants and Advisory Groups

The Act directs the Board to cooperate on an ongoing basis with professional groups of accountants that the Board has designated as a source of auditing standards and with advisory groups that the Board has convened in examining the need for changes in any standards subject to the Board’s authority. The Board is also directed to recommend issues for inclusion on the agendas of such designated professional groups of accountants or advisory groups and to take such other steps, as it deems appropriate to increase the effectiveness of the standard setting process. [Section 103(c)(1)] The Board must also respond in a timely fashion to requests from such designated professional groups and advisory groups for any changes in standards over which the Board has authority. [Section 103(c)(2)]
D. Evaluation of Standard Setting Process

The Board must include in its annual report the results of its standard setting responsibilities during the period to which the report relates. This portion of the Board’s annual report must include a discussion of the work of the Board with any designated professional groups of accountants and advisory groups, and its pending issues agenda for future standard setting projects. [Section 103(d)]

VI. Inspections of Accounting Firms

The Act requires the Board to conduct a continuing program of inspections. The purpose of these inspections is to assess the degree of compliance of each registered public accounting firm, and associated persons of that firm, with the Act, the rules of the Board, the rules of the Commission, and professional standards, in connection with its performance of audits, issuance of audit reports, and related matters involving issuers. [Section 104(a)]

Regarding the Board’s inspection program, the Senate Committee Report states:

Virtually every witness who addressed the details of auditor oversight agreed on the critical need for a regular and comprehensive review, by an independent body of inspectors, of each audit firm’s compliance with audit standards and procedures. A program of inspections is essential to identify problems in firm procedures, training, and ‘culture’ before those problems can produce audit failures that trigger large investor losses and threaten confidence in the capital markets. [Senate Committee Report at 9]

A. Inspection Frequency

Inspections must be conducted annually with respect to each registered public accounting firm that regularly provides audit reports for more than 100 issuers and not less frequently than once every three years with respect to registered public accounting firms that regularly provides audit reports for 100 or fewer issuers. The Board may, by rule, adjust this inspection schedule if it finds that different inspection schedules are consistent with the purposes of the Act, the public interest, and the protection of investors. [Section 104(b)(1)]

The Board may conduct special inspections at the request of the Commission or upon its own motion. [Section 104(b)(2)]

Under its proposed rules, the Board will conduct two types of inspections of registered public accounting firms – “regular” inspections and “special” inspections. [Proposed PCAOB Rules 4001 and 4002] Regular inspections will take place at regular intervals – in general, either annually or triennially -- consistent with Section 104(b)(1) of the Act. [Proposed PCAOB Rule 4003] Special inspections are not subject to an inspection schedule and will be conducted at such time as is necessary or appropriate concerning the issue specified by the Board in connection with its authorization of the special inspection. [Proposed PCAOB Rule 4002]
B. Inspection Objectives and Procedures

The Act requires the Board, in accordance with its rules, to take the following steps in each inspection [Section 104(c)] --

- identify any act or practice or omission to act by the registered public accounting firm, or by any associated person thereof, revealed by such inspection that may be in violation of the Act, the rules of the Board, the rules of the Commission, the firm’s own quality control policies, or professional standards;

- report any such act, practice, or omission, if appropriate, to the Commission and each appropriate State regulatory authority; and

- begin a formal investigation or take disciplinary action, if appropriate, with respect to any such violation, in accordance with the Act and the rules of the Board.

Under the Board’s proposed rules, if the Board determines that an inspection of a registered public accounting firm reveals a possible violation as described in Section 104(c) of the Act by the registered public accounting firm, any of its associated persons, or any other person, the Board, will, if appropriate (1) report the possible violation to the Commission and each state or other authority that has issued a license or certification number authorizing such person or firm to engage in the business of auditing or accounting, and (2) commence an investigation or a disciplinary proceeding in accordance with the Act and under its rules. [Proposed PCAOB Rule 4004]
In conducting an inspection of a registered public accounting firm, the Act directs the Board to take the following steps [Section 104(d)] --

- inspect and review selected audit and review engagements of the firm (which may include audit engagements that are the subject of ongoing litigation or other controversy between the firm and third parties), performed at various offices and by various associated persons of the firm, as selected by the Board;

- evaluate the sufficiency of the quality control system of the firm, and the manner of the documentation and communication of that system by the firm; and

- perform such other testing of the audit, supervisory, and quality control procedures of the firm as are necessary or appropriate in light of the purpose of the inspection and the responsibilities of the Board.

The Board’s proposed rules provide that a regular inspection will include, but is not limited to, the steps and procedures as specified in Sections 104(d)(1) and (2) of the Act and any other tests of the audit, supervisory, and quality control procedures of the firms as the Director of the Division of Registration and Inspections or the Board determines appropriate. [Proposed PCAOB Rule 4001]

The rules of the Board may require the retention by registered public accounting firms for inspection purposes of records in addition to those records otherwise required to be retained under the Act. [Section 104(e)] PCAOB Release No. 2003-013 states:
The Board is reserving this rule [on record retention and availability] in anticipation of issuing standards on record retention as part of its standard setting process once it has experience with its inspection program.

C. Board Review of Draft Inspection Reports

The rules of the Board must provide a procedure for the review of and response to a draft inspection report by the registered public accounting firm under inspection. The Board may take such action with respect to such response as it considers appropriate (including revising the draft report or continuing or supplementing its inspection activities before issuing a final report). Any such accounting firm response, appropriately redacted to protect information reasonably identified by the accounting firm as confidential, must be attached to and made part of the inspection report. [Section 104(f)]

Under the Board’s proposed rules, at the conclusion of an inspection, the Direction of the Division of Registration and Inspections must submit to the Board a written draft report. The rules set forth the process by which a draft inspection report will be submitted to a firm under review in order that the firm may submit any comments or other views concerning the draft report. [Proposed PCAOB Rules 4007(a) and (b)]

D. Final Inspection Reports

A written report of the findings of the Board with respect to each inspection must be transmitted to the Commission and each appropriate State regulatory authority, accompanied by any letter or comments by the Board or the inspector, and any letter of response from the registered public accounting firm. [Section 104(g)(1)] Such final
inspection reports are to be available in appropriate detail to the public, except that [Section 104(g)(2)] --

- no portion of an inspection report that deals with criticisms of or potential defects in the quality control systems of the firm under inspection will be made public if those criticisms or defects are addressed by the firm, to the satisfaction of the Board, not later than 12 months after the date of the report; and

- the public availability of inspection reports is also subject to the provisions of Section 105(b)(5)(A) of the Act, which states that all documents and information prepared or received by the Board in connection with an inspection are "confidential and privileged as an evidentiary matter."

Under its proposed rules, the Board must transmit a copy of the final inspection report to the firm that is the subject of the report, to the Commission, and in appropriate detail, to each state, agency, board or other authority that has issued a license or certification number authorizing the firm to engage in the business of auditing or accounting. [Proposed PCAOB Rule 4008]

Consistent with Section 104(g)(2), proposed Rule 4009 provides that, no later than 12 months after the issuance of the Board's final inspection report, firms may submit to the Director of the Division of Registration and Inspections evidence that they have improved such quality control systems, and remedied such defects. After reviewing such evidence, the Director must advise the firm whether he or she will recommend to the Board that the firm has satisfactorily addressed the criticisms or defects in the quality control system of the firm identified in the final inspection report and, if not, why not. [Proposed PCAOB Rule 4009(a)]
Further, the Board will make public those portions of a final inspection report dealing with such criticisms and defects if the firm fails to address those matters to the Board’s satisfaction within 12 months of the issuance of the final inspection report. [Proposed PCAOB Rule 4009(b)] Proposed Rule 4009(c) specifically addresses the timing of such public disclosure.

E. Commission Review

A registered public accounting firm may seek review by the Commission of a final inspection report. Review is available, pursuant Commission rules, if the firm [Section 104(h)(1)] --

- has provided the Board with a response, pursuant to the Board’s rules, to the substance of particular items in a draft inspection report, and disagrees with the assessments contained in any final report subsequently issued by the Board; or

- disagrees with the determination of the Board that criticisms or defects identified in an inspection report have not been addressed to the satisfaction of the Board within 12 months of the date of the inspection report.

Commission review may be sought during the 30-day period following the date of the event giving rise to the review. [Section 104(h)(3)] Any decision of the Commission thereon is not subject to judicial review. [Section 104(h)(2)]
VII. Investigations and Disciplinary Proceedings

The Act directs the Board to establish, by rule, fair procedures for the investigation and discipline of registered public accounting firms and associated persons of such firms. [Section 105(a)]

On July 28, 2003, the Board proposed rules on investigations and hearings in disciplinary proceedings, pursuant to Section 105 of the Act.\(^{20/}\) [PCAOB Release No. 2003-0012 (July 28, 2003)]

A. Investigations

1. Authority

The Board may conduct an investigation of any act or practice, or omission to act, by a registered public accounting firm, any associated person of such firm, or both, that may violate any provision of the Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under the Act, or professional standards, regardless of how the act, practice, or omission is brought to the attention of the Board. [Section 105(b)(1)]

The Board's rules provide for two types of Board investigative matters—informal inquiries and formal investigations and provide for the Board and its staff to

\(^{20/}\) PCAOB Rulemaking Docket Matter No. 005. The comment period on the proposed rules on investigations and adjudications closes on August 18, 2003.
undertake such matters. [Proposed PCAOB Rules 5100 through 5112]

2. Testimony and Document Production

In addition to other actions the Board determines to be necessary or appropriate, the rules of the Board may [Section 105(b)(2)] --

- require the testimony of the firm, or of any person associated with a registered public accounting firm, with respect to any matter that the Board considers relevant or material to an investigation;

- require the production of audit work papers and any other document or information in the possession of a registered public accounting firm or any associated person thereof, wherever domiciled, that the Board considers relevant or material to the investigation, and may inspect the books and records of such firm or associated person to verify the accuracy of any documents or information supplied;

- request testimony of, and production of any document in the possession of, any other person, including any client of a registered public accounting firm that the Board considers relevant or material to a Board investigation, with appropriate notice, subject to the needs of the investigation, as permitted under the rules of the Board; and

- provide for procedures to seek issuance by the Commission of a subpoena to require the testimony of, and production of any document in the possession of, any person, including any client of a registered public accounting firm, that the
Board considers relevant or material to a Board investigation.

The Board’s proposed rules implement the Board’s authority under Section 105(b)(2) of the Act to seek testimony and documents. [Proposed PCAOB Rules 5102 through 5105]

3. Non-Cooperation with Investigations

If a registered public accounting firm or any associated person thereof refuses to testify, produce documents, or otherwise cooperate with the Board in an investigation, the Board may [Section 105(b)(3)(A)] --

- suspend or bar such person from being associated with a registered public accounting firm, or require the registered public accounting firm to end such association;

- suspend or revoke the registration of the public accounting firm; and

- invoke such other lesser sanctions as the Board considers appropriate, and as specified by rule of the Board.

The Board may institute a disciplinary proceeding for non-cooperation with an investigation if it appears to the Board that a registered public accounting firm or an associated person may have failed to comply with an accounting board demand, given false testimony, or otherwise failed to cooperate in connection with an investigation. [Proposed PCAOB Rule 5200] PCAOB Release No. 2003-012 states that “a disciplinary proceeding for non-cooperation will proceed generally according to the hearing procedures set out in the Board’s rules * * * [but]
will generally be a streamlined proceeding focused on a narrow issue.

Any such Board action is reviewable by the Commission on the same terms as a final disciplinary sanction. [Section 105(b)(3)(B)]

4. Coordination and Referral of Investigations

The Board must notify the Commission of any pending Board investigation involving a potential violation of the securities laws, and thereafter coordinate with the Commission's Division of Enforcement, as necessary to protect any ongoing Commission investigation. [Section 105(b)(4)(A)]

The Board may also refer an investigation (i) to the Commission; (ii) to any other Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act), in the case of an investigation that concerns an audit report for an institution that is subject to the jurisdiction of such regulator; and (iii) at the direction of the Commission, to the Attorney General of the United States, the a state attorney general, and to the appropriate State regulatory authority. 21/ [Section 105(b)(4)(B)]

The Board’s proposed rules set forth a procedure for coordination and referral of investigations to the Commission and other federal regulators, the U.S. attorney general, the attorney general of one or more states, or an appropriate state regulatory authority. [Proposed PCAOB Rule 5112]

21/ The entities listed in (i) through (iii) above are referred to in this outline as “referral agencies.”
5. **Use of Documents**

All documents and information prepared or received by or specifically for the Board, and deliberations of the Board and its employees and agents, in connection with a Board inspection or with an investigation, are confidential and privileged as an evidentiary matter (and are not subject to civil discovery or other legal process) in any proceeding in any Federal or State court or administrative agency. Such documents and information are also exempt from disclosure, in the hands of an agency or establishment of the Federal Government, under the Freedom of Information Act (5 U.S.C. 552a), or otherwise, unless and until presented in connection with a public proceeding or released in accordance with the provisions of the Act governing disciplinary proceedings. [Section 105(b)(5)(A)]

Without the loss of its status as confidential and privileged in the hands of the Board, all such information may be made available to the Commission; and, in the discretion of the Board, to any of the other referral agencies, each of which must maintain such information as confidential and privileged. [Section 105(b)(5)(B)]

Consistent with Section 105(b)(5)(A) of the Act, the Board’s proposed rules provide for the confidentiality of investigative records. [Proposed PCAOB Rule 5108]

6. **Immunity**

Any employee of the Board engaged in carrying out an investigation under the Act is immune from any civil liability arising out of such investigation in the same manner and to the same extent as an employee of the Federal Government in similar circumstances. [Section 105(b)(6)]
B. Disciplinary Procedures

1. Notification, Recordkeeping, and Hearings

Under the rules of the Board, in any proceeding by the Board to determine whether a registered public accounting firm, or an associated person thereof, should be disciplined, the Board must [Section 105(c)(1)] --

- bring specific charges with respect to the firm or associated person;

- notify such firm or associated person of, and provide to the firm or associated person an opportunity to defend against, such charges; and

- keep a record of the proceedings.

Hearings to determine whether a registered public accounting firm, or an associated person thereof, should be disciplined are not public, unless otherwise ordered by the Board for good cause shown, with the consent of the parties to such hearing. [Section 105(c)(2)]

In PCAOB Release No. 2003-012, the Board states:

Most of the Board's disciplinary proceedings will likely involve apparent violations of the securities laws, or of the Board's rules and professional standards, that are discovered as a result of Board inspections or investigations. The Board's disciplinary process, however, will also address two other situations – the failure of registered public accounting firms and their associated persons to cooperate with Board investigations and the failure of registered public accounting firms or their
supervisory personnel reasonably to supervise associated persons who have committed violations.

The Board's proposed rules codify the three types of disciplinary proceedings the Board will conduct, as described above. [Proposed PCAOB Rules 5200 through 5207] Consistent with Section 105(c) of the Act, the proposed rules provide for a record of every hearing to be kept, and for hearings to be nonpublic, unless otherwise ordered by the Board. [Proposed PCAOB Rules 5202 and 5203] In disciplinary proceedings, consistent with Section 105(c)(2) of the Act, the Board will order a hearing to be public only upon a showing of good cause and the consent of the parties to the hearing. [Proposed PCAOB Rule 5203]

2. Statement Supporting Sanction

A determination by the Board to impose a sanction must be supported by a statement setting forth [Section 105(c)(3)] --

- each act or practice in which the registered public accounting firm, or associated person, has engaged (or omitted to engage), or that forms a basis for all or a part of such sanction;

- the specific provision of the Act, the securities laws, the rules of the Board, or professional standards which the Board determines has been violated; and

- the sanction imposed, including a justification for that sanction.
3. **Sanctions**

If the Board finds, based on all of the facts and circumstances, that a registered public accounting firm or associated person thereof has engaged in any act or practice, or omitted to act, in violation of the Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under the Act, or professional standards, the Board may impose such disciplinary or remedial sanctions as it determines appropriate, including [Section 105(c)(4)] --

A. Temporary suspension or permanent revocation of registration;

B. Temporary or permanent suspension or bar of a person from further association with any registered public accounting firm;

C. Temporary or permanent limitation on the activities, functions, or operations of such firm or person (other than in connection with required additional professional education or training);

D. A civil money penalty for each such violation, in an amount equal to (i) not more than $100,000 for a natural person or $2,000,000 for any other person; and, in the case of intentional or knowing misconduct, (ii) not more than $750,000 for a natural person or $15 million for any other person;

E. Censure;
F. Required additional professional education or training; or

G. Any other appropriate sanction provided for in the rules of the Board.

The sanctions and penalties set forth in subparagraphs A. through C. and D.ii. above only apply to [Section 105(c)(5)] --

- intentional or knowing conduct, including reckless conduct, that results in violation of applicable statutory, regulatory, or professional standards; or

- repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.

Proposed Rule 5300 codifies those sanctions specifically described in Section 105(c)(4) of the Act and adds four additional sanctions related to appointment of an independent monitor to observe and report on compliance, appointment of counsel or another consultant to design policies to effectuate compliance, requiring adoption or implementation of certain policies or other undertakings, and requiring a firm to obtain an independent review and report on one or more audit engagements. This rule also includes sanctions based on disciplinary proceedings relating to noncooperation with an investigation, pursuant to Section 105(b) of the Act, including suspension or revocation of a firm's registration, a suspension or bar of an associated person, certain civil money penalties, a censure, appointment of a special master or independent monitor to monitor and report on compliance accounting board demands, and authorization for a hearing officer to retain jurisdiction to
monitor compliance with accounting board demands and to rule on future disputes. [Proposed PCAOB Rule 5300]

4. Failure to Supervise

The Board may impose sanctions on a registered accounting firm, or upon the supervisory personnel of such firm, if the Board finds that [Section 105(c)(6)(A)] --

- the firm has failed reasonably to supervise an associated person, either as required by the rules of the Board relating to auditing or quality control standards, or otherwise, with a view to preventing violations of the Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission under the Act, or professional standards; and

- such associated person commits a violation of the Act, or any of such rules, laws, or standards.

No associated person of a registered public accounting firm may be deemed to have failed reasonably to supervise any other person for purposes of subparagraph (A), if [Section 105(c)(6)(B)] --

- there have been established in and for that firm procedures, and a system for applying such procedures, that comply with applicable rules of the Board and that would reasonably be expected to prevent and detect any such violation by such associated person; and
• such person has reasonably discharged the duties and obligations incumbent upon that person by reason of such procedures and system, and had no reasonable cause to believe that such procedures and system were not being complied with.

5. **Effect of Suspension**

No person that is suspended or barred from association with a registered public accounting firm may willfully become or remain associated with any registered public accounting firm. No registered public accounting firm that knew, or, in the exercise of reasonable care should have known, of the suspension or bar, may permit such an association, without the consent of the Board or the Commission. [Section 105(c)(7)(A)]

No person that is suspended or barred from being associated with an issuer may willfully become or remain associated with any issuer in an accountancy or a financial management capacity. No issuer that knew, or in the exercise of reasonable care should have known, of such suspension or bar, may permit such an association, without the consent of the Board or the Commission. [Section 105(c)(7)(B)]

The Board’s proposed rules address the effect of sanctions on persons and on registered firms, consistent with Section 105(c)(7)(A) of the Act. [Proposed PCAOB Rule 5301]

C. **Reporting of Sanctions**

If the Board imposes a disciplinary sanction, the Board must report the sanction to the Commission; any appropriate State regulatory authority or any foreign accountancy licensing board with which such firm or person
is licensed or certified; and the public (once any stay on the imposition of such sanction has been lifted). [Section 105(d)(1)] The information reported includes [Section 105(d)(2)] --

- the name of the sanctioned person;

- a description of the sanction and the basis for its imposition; and

- such other information as the Board deems appropriate.

D. Stay of Sanctions

Application to the Commission for review, or the institution by the Commission of review, of any disciplinary action of the Board operates as a stay of any such disciplinary action. The Commission may order (summarily or after notice and opportunity for hearing on the question of a stay, which hearing may consist solely of the submission of affidavits or presentation of oral arguments) that the stay terminate. The Commission must establish an expedited procedure for consideration and determination of the question of the duration of a stay pending review of any disciplinary action of the Board under this subsection. [Section 105(e)]

Consistent with Section 105(e) of the Act, the Board’s proposed rules provide for an automatic stay of any final disciplinary action until the later of (a) Commission action to dissolve the stay, or (b) the expiration of the period during which, on its own motion, or upon application pursuant to Section 19(d)(2) of the Exchange Act, the Commission may institute review of the action. [Proposed PCAOB Rule 5207]
VIII. Foreign Auditing Firms

The Senate Committee Report summarizes the philosophy of the Act with respect to foreign auditing firms:

[T]he Committee believes that there should be no difference in treatment of a public company's auditors under the bill simply because of a particular auditor's place of operation. Otherwise, a significant loophole in the protection offered U.S. investors would be built into the statutory system.

Thus, accounting firms organized under the laws of countries other than the United States that issue audit reports for public companies subject to the U.S. securities laws are covered by the bill in the same manner as domestic accounting firms, subject to the exemptive authority of both the Board and the SEC. [Senate Committee Report at 11]

A. Applicability to Certain Foreign Firms

1. Foreign Firms That Issue Audit Reports on U.S. Issuers

The term "foreign public accounting firm" means a public accounting firm that is organized and operates under the laws of a foreign government or political subdivision thereof. [Section 106(d)] Any foreign public accounting firm that prepares or furnishes an audit report with respect to any issuer, is subject to the Act and the rules of the Board and the Commission issued under the Act, in the same manner and to the same extent as a U.S. public accounting firm. However, a foreign firm’s registration with the Board
does not by itself provide a basis for subjecting such a foreign public accounting firm to the jurisdiction of the Federal or State courts, other than with respect to controversies between such firm and the Board. [Section 106(a)(1)]

2. **Foreign Firms That Participate in Audits of U.S. Issuers**

The Board may, by rule, determine that a foreign public accounting firm (or a class of such firms) that does not issue audit reports nonetheless plays such a substantial role in the preparation and furnishing of such reports for particular issuers, that it is necessary or appropriate, in light of the purposes of the Act and in the public interest or for the protection of investors, that such firm (or class of firms) should be treated as a public accounting firm (or firms) for purposes of registration under, and oversight by the Board in accordance with, the Act. [Section 106(a)(2)]

B. **Production of Audit Workpapers**

1. **Foreign Firm Consents**

If a foreign public accounting firm issues an opinion or performs material services upon which a registered public accounting firm relies in issuing all or part of any audit report, that foreign public accounting firm is deemed to have consented [Section 106(b)(1)] --

- to produce its audit workpapers to the Board or the Commission in any investigation by either body with respect to that audit report; and

- to be subject to the jurisdiction of the courts of the United States for purposes of enforcement of any request for production of such workpapers.
2. **Domestic Firm Consents**

A registered public accounting firm that relies upon the opinion of a foreign public accounting firm is deemed [Section 106(b)(2)]--

- to have consented to supplying the audit workpapers of that foreign public accounting firm in response to a request for production by the Board or the Commission; and

- to have secured the agreement of that foreign public accounting firm to such production, as a condition of its reliance on the opinion of that foreign public accounting firm.

C. **Exemption Authority**

The Commission, and the Board, subject to the approval of the Commission, may, by rule, regulation, or order, and as the Commission (or Board) determines necessary or appropriate in the public interest or for the protection of investors, either unconditionally or upon specified terms and conditions, exempt any foreign public accounting firm, or any class of such firms, from any provision of the Act or the rules of the Board or the Commission. [Section 106(c)]

D. **Foreign Firm Registration Issues**

During the comment period on the Board’s public accounting firm registration rules, the Board received numerous comment letters from public accounting firms, foreign governments and foreign professional accounting associations. On March 31, 2003, the Board also held a public roundtable meeting to discuss special issues raised by registration and oversight of non-U.S. firms, at which 14
representatives of foreign governments, non-U.S. public accounting firms and professional organizations, and U.S. institutional investors participated.

In general, foreign accounting firms and foreign accounting regulators opposed the registration of non-U.S. accounting firms that audit U.S. public companies and urged that the Board or the Commission exempt such firms. These commenters expressed concern that registration of non-U.S. public accounting firms (1) would be duplicative of existing or planned home-country auditor oversight programs, (2) would require information, the disclosure of which would violate foreign laws on confidentiality, data protection and privacy, (3) would require information that does not have clear equivalents in non-U.S. jurisdictions, (4) would require accumulation of information not already compiled and not readily available, and (5) would lessen competition among public accounting firms by discouraging some firms from registering.

In PCAOB Release No. 2003-007 (May 6, 2003), the Board determined not to exempt from registration any public accounting firm, domestic or foreign, that prepares or issues, or plays a substantial role in the preparation or issuance of, any audit report on financial statements that are filed in the United States. The Board stated:

Registration is the predicate to all the Board's other oversight programs – compliance with auditing and other professional standards, inspections, and discipline – and therefore an exemption from registration would be tantamount to a complete exemption from any oversight by the Board. * * * [T]he Board, based on the provisions of the Act and on pre-Act requirements and practice, is unable to conclude that a general exemption for foreign
public accounting firms that audit, or participate in audits of, U.S. public companies is appropriate.

However, the Board also adopted certain measures to accommodate the special needs of foreign registrants. Further, the Board announced that it would seek to coordinate its activities with foreign regulators in order to minimize the burdens imposed on applicants based in other jurisdictions.

In Exchange Act Release No. 48180, the Commission, supporting the Board's position on the registration of non-U.S. audit firms, stated:

The Board has taken an important step in its mandate under the Act by proposing rules regarding registration of non-U.S. audit firms that prepare, issue, or play a substantial role in the preparation or issuance of, audit reports relating to U.S. public companies. This step has raised concerns in the international community, and the Board has made efforts to address those concerns, through its roundtable meeting in March, through its public comment process and through meetings and discussions with foreign regulators. In response to these concerns, the Board made significant accommodations in its proposal, especially with regard to non-U.S. accounting firms, including changes eliminating the potential conflicts of law raised by the registration system, narrowing the scope of information to be provided, and extending the deadline for foreign firms to register. This approach is similar to the approach the Commission has
taken in implementing other provisions of the Act, by allowing for certain accommodations.

1. **Rule 2105**

Many commenters suggested that registration of non-U.S. firms would require information, the disclosure of which would violate non-U.S. laws, particularly those related to confidentiality, data protection and privacy. In response to this concern, the Board adopted Rule 2105 and corresponding instructions in Form 1. Rule 2105 allows an applicant to withhold information from its application for registration where disclosure of the information would cause the applicant to violate non-U.S. laws. An applicant that claims that submitting information as part of its application would cause it to violate non-U.S. laws must identify the information and include, as an exhibit to Form 1 –

- a copy of the relevant portion of the conflicting non-U.S. law;

- a legal opinion that submitting the information would cause the applicant to violate the conflicting non-U.S. law; and

- an explanation of the applicant's efforts to seek consents or waivers to eliminate the conflict, if the withheld information could be provided to the Board with a consent or a waiver, and a representation that the applicant was unable to obtain such consents or waivers to eliminate the conflict.
2. **Roster of Accountants Associated with Foreign Firms**

In order to address foreign privacy concerns, the Board narrowed the list of associated accountants that must be disclosed in the case of a non-U.S. applicant. As revised, Form 1 requires non-U.S. accounting firms to a list only those accountants who are proprietors, partners, principals, shareholders, officers or managers of the applicant and who each provided at least 10 hours of audit services for any issuer during the last calendar year. [PCAOB Form 1, note to Item 7.1]

3. **Delay in Foreign Firm Registration**

In response to concerns that registration of non-U.S. firms would require accumulation of information not already compiled and not readily available, the Board has allowed an additional 180 days for foreign firms to register with the Board. In PCAOB Release No. 2003-007 (May 6, 2003), the Board stated:

While the Board believes that it must require registration of non-U.S. firms, it also recognizes that it must be flexible about how registration operates in the case of those firms and that it may not be practical to treat foreign accounting firms as if they were, for purposes of the Board's regulation, in all respects the same as U.S.-based firms. The Board is prepared to work with its foreign counter-parts to find ways to accomplish the goals of the Act without subjecting foreign firms to unnecessary burdens or conflicting requirements. Where possible, the Board will seek to build compliance with its requirements on compliance with foreign regulatory
regimes. The proposed 180-day deferral of foreign firm registration will afford the Board the opportunity to explore ways of accomplishing that goal with non-U.S. accounting oversight bodies. [PCAOB Release No. 2003-007 (May 6, 2003) at 20]

E. Oversight of Foreign Firms

In PCAOB Release No. 2003-012 (July 28, 2003) and PCAOB Release No. 2003-013 (July 28, 2003), the Board stated:

The nature and scope of the Board’s oversight over non-U.S. accounting firms that audit the financial statements of U.S. public companies will be the subject of dialogue between the Board and its foreign counterparts. The Board is committed to finding ways of accomplishing the goals of the Act without subjecting non-U.S. firms to unnecessary burdens or conflicting requirements.

IX. Securities and Exchange Commission Oversight of the Board

The Commission has oversight and enforcement authority over the Board. The Commission has authority to require that the Board maintain records, and authority to inspect the Board, as fully as if the Board were a "registered securities association" for purposes of provisions of Section 17(a)(1) of the Exchange Act. [Section 107(a)]
A. Oversight of Board Rulemaking

1. Definitions

The term "rules of the Board" means the bylaws and rules of the Board (as submitted to, and approved, modified, or amended by the Commission), and those stated policies, practices, and interpretations of the Board that the Commission, by rule, may deem to be rules of the Board, as necessary or appropriate in the public interest or for the protection of investors. [Section 2(a)(13)] The term "proposed rule" means any proposed rule of the Board, and any modification of any such rule. [Section 107(b)(1)]

2. Commission Approval of Board Rules

No rule of the Board becomes effective without prior approval of the Commission. (Section 103(a)(3) of the Act contains an exception with respect to initial or transitional auditing standards.) [Section 107(b)(2)] The Commission must approve a proposed rule, if it finds that the rule is consistent with the requirements of the Act and the securities laws, or is necessary or appropriate in the public interest or for the protection of investors. [Section 107(b)(3)]

The provisions of Section 19(b) of the Exchange Act, which govern the Commission’s review and approval or disapproval of the rules of certain securities industry self-regulatory organizations, apply to proposed rules of the Board, as fully as if the Board were a "registered securities association" (with certain modifications to reflect the purposes and responsibilities of the Board). [Section 107(b)(4)]
3. **Commission Authority to Amend Rules of the Board**

Similarly, the provisions of Section 19(c) of the Exchange Act, which govern the Commission's authority to abrogate, delete, or add to the rules of certain securities industry self-regulatory organizations, apply to the Board as fully as if the Board were a "registered securities association" (with certain modifications to reflect the purposes and responsibilities of the Board). [Section 107(b)(5)]

**B. Oversight of Board Disciplinary Action**

1. **Notice and Review of Board Sanctions**

The Board must promptly file notice with the Commission of any final sanction on any registered public accounting firm or on any associated person thereof. Notice must be in such form, and contain such information, as the Commission, by rule, may prescribe. [Section 107(c)(1)]

The provisions of Sections 19(d)(2) and 19(e)(1) of the Exchange Act, which govern the Commission's review of final disciplinary sanctions imposed by certain securities industry self-regulatory organizations, apply to final disciplinary sanctions imposed by the Board, as fully as if the Board were a "registered securities association" (with certain modifications to reflect the purposes and responsibilities of the Board). [Section 107(c)(2)]

2. **Commission Modification of Board Sanctions**

The Commission may enhance, modify, cancel, reduce, or require the remission of a sanction imposed by the Board upon a registered public accounting firm or associated person thereof, if the Commission, having due regard for the public interest and the protection of investors, finds, after its
review proceeding, that the Board’s sanction [Section 107(c)(3)] --

- is not necessary or appropriate in furtherance of the Act or the securities laws; or

- is excessive, oppressive, inadequate, or otherwise not appropriate to the finding or the basis on which the sanction was imposed.

C. Power to Sanction the Board

1. Rescission of Board Authority

The Commission, by rule, consistent with the public interest, the protection of investors, and the other purposes of the Act and the securities laws, may relieve the Board of any responsibility to enforce compliance with any provision of the Act, the securities laws, the rules of the Board, or professional standards. [Section 107(d)(1)]

2. Censure or Limitation of the Board

The Commission may, by order, as it determines necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act or the securities laws, censure or impose limitations upon the activities, functions, and operations of the Board, if the Commission finds, on the record, after notice and opportunity for a hearing, that the Board [Section 107(d)(2)] --

- has violated or is unable to comply with any provision of the Act, the rules of the Board, or the securities laws; or
• without reasonable justification or excuse, has failed to enforce compliance with any such provision or rule, or any professional standard, by a registered public accounting firm or an associated person thereof.

3. Censure or Removal From Office of Board Members

The Commission may, as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act or the securities laws, remove from office or censure any member of the Board, if the Commission finds, on the record, after notice and opportunity for a hearing, that such member [Section 107(d)(3)] --

• has willfully violated any provision of the Act, the rules of the Board, or the securities laws;

• has willfully abused the authority of that member; or

• without reasonable justification or excuse, has failed to enforce compliance with any such provision or rule, or any professional standard by any registered public accounting firm or any associated person.

D. Annual Report to the Commission

The Board must submit an annual report (including its audited financial statements) to the Commission, and the Commission must transmit a copy of that report to the Committee on Banking, Housing, and Urban Affairs of the Senate, and the Committee on Financial Services of the House of Representatives, not later than 30 days after the
date of receipt of that report by the Commission. [Section 101(h)]

X. Conclusion

While the Act provides a general blueprint for the discharge of the Board's responsibilities, the Board itself must fill in many of the critical details by rulemaking and administrative practice. During the early months of its operation, the Board has begun that process and has started to create a regulatory framework within which in can effectively discharge its mandate to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports for public companies. Much, however, remains to be done. It will likely be several years before the Board's regulatory structure is complete.