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SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-77787; File No. PCAOB-2016-01)

May 9, 2016

Public Company Accounting Oversight Board; Order Granting Approval of Proposed Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form and Related Amendments to Auditing Standards

I. Introduction

On January 29, 2016, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission"), pursuant to Section 107(b)[1] of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act") and Section 19(b)[2] of the Securities Exchange Act of 1934 (the "Exchange Act"), a proposal to adopt two new rules, a new form, and amendments to auditing standards to improve transparency regarding the engagement partner and other accounting firms that participate in issuer audits (collectively, the "Proposed Rules").[3] The Proposed Rules were published for comment in the

[1] 15 U.S.C. 7217(b).

[2] 15 U.S.C. 78s(b).

[3] The Board originally issued a concept release in 2009. See *Concept Release on Requiring the Engagement Partner to Sign the Audit Report*, PCAOB Release No. 2009-005 (July 28, 2009) ("Concept Release"), *available at* http://pcaobus.org/Rules/Rulemaking/Docket029/2009-07-28_Release_No_2009-005.pdf. In 2011, the Board issued proposed rules. See *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form* 2, PCAOB Release No. 2011-007 (Oct. 11, 2011) ("Proposal"), *available at* https://www.sec.gov/rules/pcaob/2016/34-77082.pdfhttp://pcaobus.org/Rules/Rulemaking/Docket029/PCAOB_Release_2011-007.pdf. Subsequently, the Board issued a re-proposal in 2013. See *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit,* PCAOB Release No. 2013-009 (Dec. 4, 2013) ("Reproposal"), *available at* http://pcaobus.org/Rules/Rulemaking/Docket029/PCAOB%20Release%20No%20%202013-009%20-%20Transparency.pdf. In 2015, the Board issued a supplemental request for comment, which ultimately formed the framework for these Proposed Rules. See *Supplemental Request for Comment: Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form*, PCAOB Release No. 2015-004 (June 30, 2015) ("Supplemental Request"), *available at* http://pcaobus.org/Rules/Rulemaking/Docket029/Release_2015_004.pdf.

Federal Register on February 16, 2016.[4] At the time the notice was issued, the Commission extended to May 16, 2016 the date by which the Commission should take action on the Proposed Rules.[5] The Commission received four comment letters in response to the notice.[6] This order approves the Proposed Rules.

II. Description of the Proposed Rules

On December 15, 2015, the Board adopted two new rules ("Rules 3210 and 3211") and Form AP to provide investors and other financial statement users with information about engagement partners and accounting firms that participate in audits of issuers.

A. Changes to PCAOB Rules and Forms

Under the Proposed Rules, for each audit report it issues for an issuer, a registered public accounting firm must file with the Board a report on Form AP that includes the following:

- The name of the engagement partner and Partner ID;[7]
- For other accounting firms[8] participating in the audit for which the responsibility for the audit is not divided:

[4] See Release No. 34-77082 (Feb. 8, 2016), 81 FR 7927 (Feb. 16, 2016).

[5] Ibid.

[6] See letters to the Commission from CFA Institute, dated February 15, 2016 ("CFA Letter"); Tom Quaadman, Senior Vice President, Center for Capital Markets Competitiveness, U.S. Chamber of Commerce, dated March 3, 2016 ("Chamber Letter"); Deloitte & Touche LLP, dated March 4, 2016 ("Deloitte Letter"); and Michael R. McMurtry, CPA, dated March 18, 2016 ("McMurtry Letter").

[7] The firm is required to assign a 10-digit Partner ID number, beginning with the Firm ID (a unique five-digit number based on the number assigned to the firm by the PCAOB at the time of registration) followed by a unique series of five digits assigned by the firm.

[8] The Board defines "other accounting firm" as (i) a registered public accounting firm other than the firm filing Form AP; or (ii) any other person or entity that opines on the compliance of any entity's financial statements with an applicable financial reporting framework.

- 5% or greater participation: The name, city and state (or, if outside the United States, the city and country) of the headquarters' office, and, when applicable, the Firm ID, and the percentage of total audit hours attributable to each other accounting firm whose participation in the audit was at least 5% of total audit hours;[9]
- Less than 5% participation: The number of other accounting firms that participated in the audit whose individual participation was less than 5% of total audit hours, and the aggregate percentage of total audit hours of such firms; and

- For other accounting firms participating in the audit for which the responsibility for the audit is divided:
  - The name, and when applicable, the Firm ID; city and state (or if outside the United States, the city and country) of the office of the other accounting firm that issued the other auditor's report; and the magnitude of the portion of the financial statements audited by the other accounting firm.

Form AP has a basic filing deadline of 35 days after the date the auditor's report is first included in a document filed with the Commission, with a shorter deadline of 10 days after the auditor's report is first included in a registration statement under the Securities Act of 1933 (the "Securities Act") filed with the Commission, such as for an initial public offering. Firms will file Form AP through the PCAOB's existing web-based Registration, Annual, and Special Reporting system.

[9] Actual hours should be used if available. If actual audit hours are unavailable, the auditor may use a reasonable method to estimate the components of this calculation.

B. Changes to PCAOB Standards

In addition to disclosing the required information on Form AP, the Proposed Rules allow an audit firm to voluntarily provide information about the engagement partner, other accounting firms, or both in the auditor's report. As a result, the Proposed Rules include amendments to PCAOB auditing standards AS 3101 (currently AU sec. 508), *Reports on Audited Financial Statements*, and AS 1205 (currently AU sec. 543), *Part of the Audit Performed by Other Independent Auditors*[10] to allow for voluntary reporting.

C. Applicability and Effective Date

The PCAOB has proposed application of the Proposed Rules to audits of all issuers, including audits of emerging growth companies ("EGCs"),[11] as discussed in Section IV. below. The Proposed Rules would not apply to audits of brokers and dealers under Exchange Act Rule 17a-5.[12] The Proposed Rules would be effective as follows:

a) Disclosure of the engagement partner: auditors' reports issued on or after January 31, 2017; and

b) Disclosure of other accounting firms: auditors' reports issued on or after June 30, 2017.

III. Comment Letters

As noted above, the Commission received four comment letters concerning the Proposed

[10] On March 31, 2015, the PCAOB adopted the reorganization of its auditing standards using a topical structure and a single, integrated numbering system that was approved by the Commission on September 17, 2015. The reorganized amendments will be effective as of December 31, 2016, and nothing precludes auditors and others from using and referencing the reorganized standards before the effective date.

[11] The term "emerging growth company" is defined in Section 3(a)(80) of the Exchange Act. 15 U.S.C. 78c(a)(80).

[12] If the broker or dealer is an issuer, the Proposed Rules would apply.

Rules. Two commenters expressed support for the Proposed Rules.[13] One commenter provided comments that were generally consistent with those provided by others throughout the PCAOB's rulemaking process and addressed by the PCAOB.[14]

In addition, one commenter raised concerns that it had previously raised in comment letters to the Board that: a) the Proposed Rules were not liability neutral; and b) the substance of the economic analysis was insufficient to justify applying the Proposed Rules to audits of EGCs.[15] In addition, this commenter raised two additional issues, including that the 10-digit partner identifying number was not subject to a notice and comment period and a suggestion that the Proposed Rules should sunset after five years, unless a post implementation review finds that the Proposed Rules promote investor protection, capital formation and competition. The commenter stated that it expressed similar concerns in previous comment letters to the PCAOB, and in its opinion, those concerns have not been resolved by the PCAOB. We discuss each of these concerns below.

a) Liability neutrality

In the release accompanying the Proposed Rules ("Final Rule Release"), the Board noted that this commenter asserted that the Board should not pursue disclosure requirements for the engagement partner and other participants in the audit unless it can be done in a "liability neutral" way.[16] The Board explained that its purpose with the Proposed Rules is not to expose auditors to

[13] See CFA Letter and Deloitte Letter.

[14] See McMurtry Letter. The Commission believes that the Board has reasonably responded to these comments in its rulemaking process.

[15] See Chamber Letter.

[16] See comment letter of U.S. Chamber of Commerce's Center for Capital Markets Competitiveness, August 31, 2015 *available at* http://pcaobus.org/Rules/Rulemaking/Docket029/031d_Chamber.pdf. This letter was also referenced in the Chamber Letter.

additional liability, and consistent with that purpose, it has endeavored to mitigate any additional liability consequences that may stem from the Proposed Rules. However, the Board also stated in the Final Rule Release that it does not agree with the premise that it should not seek to achieve the anticipated benefits of a new rule – here, increased transparency and accountability for key participants in the audit – unless it can be certain that its actions will not affect liability in any way. On the whole, the Board believes it has appropriately addressed concerns regarding liability consequences of its proposal in a manner compatible with the objectives of this rulemaking, and in view of the rulemaking's anticipated benefits.

Since the Concept Release, the Board has sought and considered commenters' views on the liability effect of its proposed amendments, has taken steps with the intent not to increase auditors' liability risk, and has tried to mitigate this possibility to the extent it would be consistent with its policy objectives. In the Reproposal, the Board included a detailed discussion on potential liability considerations of its proposed amendments, including liability under Section 11 of the Securities Act of 1933 ("Securities Act") and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The Board has also indicated that it takes seriously commenters' concerns about the potential effects on auditor liability, has engaged in its own review of the relevant statutory provisions and case law and has kept the Commission staff advised of its thoughts on these issues, as commenters suggested.

The Board has specifically tailored the Proposed Rules to address, in part, potential liability considerations raised by commenters. In the Supplemental Request, the Board acknowledged that some commenters on the Reproposal expressed concern that identifying the engagement partner and other participants in the audit in the auditor's report could create both legal and practical issues

under the federal securities laws by increasing the named parties' potential liability and by requiring their consent if the auditors' reports naming them were included in, or incorporated by reference into, registration statements under the Securities Act. The Board also acknowledged that some commenters expressed concerns about the possible litigation risk under Section 10(b) of the Exchange Act and Rule 10b-5 thereunder of the engagement partner's name appearing in the auditor's report. The Board further noted that many commenters urged the Board to proceed with the new disclosure requirements, if it determined to do so, by mandating disclosure on a newly created PCAOB form (or consider other alternative locations) as a means of responding to liability concerns. In response to these concerns, the Supplemental Request proposed disclosure on new Form AP, an alternative location outside the auditor's report, and specifically sought comment on whether disclosure on Form AP would mitigate commenters' concerns about liability-related consequences.

In the Final Rule Release, the Board further acknowledged commenters' concerns that public identification of key audit participants, particularly in the auditor's report, could impact the potential liability or litigation risks of those identified. In particular, the Board noted that it sought comment throughout the rulemaking process on various means of disclosure – from an engagement partner's signature on the auditor's report, to disclosure in the auditor's report, to disclosure on Form AP – in part to respond to those concerns. The Board stated that it believes the final rules accomplish its disclosure goals while appropriately addressing concerns raised by commenters about liability. The Board also observed that disclosure on Form AP should not raise potential liability concerns under Section 11 of the Securities Act or trigger the consent requirements of Section 7 of the Act because the engagement partner and other accounting firms would not be

named in a registration statement or in any document incorporated by reference into one.[17] While the Board recognized that commenters expressed mixed views on the potential for liability under Exchange Act Section 10(b) and Rule 10b-5 and the ultimate resolution of Section 10(b) liability is outside its control, the Board stated that it does not believe any such risks warrant not proceeding with the Form AP approach.

The Commission believes that the Board has provided sufficient notice of potential liability consequences of the Proposed Rules, has provided sufficient opportunity for public comment on these issues, and has reasonably responded to such concerns. Specifically, the Commission believes the Board has appropriately considered concerns related to liability neutrality as part of the Final Rule Release and taken reasonable steps to address the comments raised with respect to liability considerations in the Proposed Rules.

b) Economic analysis

The Chamber Letter also suggested that the Board's economic analysis was insufficient to justify applying the Proposed Rules to audits of EGCs. This commenter, however, did not indicate why the economic analysis was insufficient, other than to say that the analysis and the application of the Proposed Rules to EGCs are "contrary to the intent of Congress [in passing the Jumpstart Our Business Startups Act]." The Board presented, and sought comment on, an economic analysis in the Reproposal. Further, in response to comments on the economic analysis provided in connection with the Reproposal, the Board revised its analysis, and sought comment on, an economic analysis as presented in the Supplemental Request. The economic analysis in the Supplemental Request set forth: (1) a description of the need for the standard-setting and how the

[17] This assumes the auditor does not voluntarily choose to do so by including relevant disclosures in the auditor's report.

Proposed Rules address that need; (2) the baseline to consider the economic impacts of the Proposed Rules; (3) the economic impacts of the Proposed Rules including benefits, costs, effects on different categories of audit firms and smaller companies, and responses to comments received on the economic analysis included with the Reproposal; and (4) economic considerations pertaining to audits of EGCs, including efficiency, competition and capital formation. In its Final Rule Release, the Board further discussed the economic considerations of the Proposed Rules and included a separate discussion within the economic analysis devoted to potential liability consequences.

The Commission notes that the Board provided a qualitative analysis that took into account the views of commenters. As the Board explained, there was limited research and data available regarding economic costs and benefits of the Proposed Rules for U.S. companies, making reliable quantification difficult. As the Board further explained, as part of its rulemaking process through the issuance of the Proposed Rules, the Board requested input from commenters. While commenters provided views on issues pertinent to economic considerations, including potential benefits and costs, they did not provide empirical data. The Commission believes that the Board's economic analysis reasonably addresses the comments raised and, as further discussed below, is sufficient to make a determination to apply the Proposed Rules to the audits of EGCs.

c) 10-digit partner identifying number

The Chamber Letter also noted that the Board added the 10-digit partner identifying number as part of the Final Rule Release without subjecting it to notice and comment. The Board added the 10-digit partner identifying number to the Proposed Rules in response to suggestions made by

two commenters on the Supplemental Request.[18] These commenters suggested that a unique partner identifier would help unambiguously identify partners and provide clear identification of auditors with the same or similar names. The Commission's own notice and comment period on the Proposed Rules provided an opportunity for commenters to address concerns they may have had with the partner identifying number. No commenter identified any substantive concerns with the application of the identifying number. The Commission believes that the feedback received by the Board on the Supplemental Request and the opportunity for public comment on the Commission's notice of the Proposed Rules provide sufficient basis for the Board to include the 10-digit partner identifying number in the Proposed Rules.

d) Sunset provision

Finally, the Chamber Letter also suggested that the Proposed Rules should sunset after five years, unless a post implementation review finds that the Proposed Rules promote investor protection, capital formation and competition. The Board stated in the Final Rule Release that it has considered feedback received on the concept release issued by the Commission on Possible Revisions to Audit Committee Disclosures ("SEC Concept Release")[19] in developing the Proposed Rules. It also stated that it will continue to monitor the provisions included in the Proposed Rules to determine if revisions should be made in the future. In addition, the Board has a process in place

[18] See letters from the Auditing Standards Committee of the Auditing Section of the American Accounting Association, dated August 30, 2015, available at http://pcaobus.org/Rules/Rulemaking/Docket029/024d_AAA.pdf and Maureen McNichols, dated August 31, 2015, *available at* http://pcaobus.org/Rules/Rulemaking/Docket029/037d_McNichols.pdf.

[19] See *Possible Revisions to Audit Committee Disclosures,* Release No. 33-9862 (July 1, 2015), *available at*: http://www.sec.gov/rules/concept/2015/33-9862.pdf.

to perform post-implementation reviews for its standards and rules.[20] Therefore, the Commission does not believe a specific sunset provision is necessary in the Proposed Rules.

IV. The PCAOB's EGC Request

Section 103(a)(3)(C) of the Sarbanes-Oxley Act requires that any rules of the Board "requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements (auditor discussion and analysis)" shall not apply to an audit of an EGC. The Board's Proposed Rules do not fall into this category of rules.[21] Section 103(a)(3)(C) further provides that "[a]ny additional rules" adopted by the PCAOB after April 5, 2012 do not apply to EGCs "unless the Commission determines that the application of such additional requirements is necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation." The Proposed Rules fall within this category of additional rules and thus the Commission must make a determination under the statute about the applicability of the Proposed Rules to EGCs. Having considered those statutory factors, and as explained further herein, the Commission finds that applying the Proposed Rules to audits of EGCs is necessary or appropriate in the public interest.

In proposing application of the Proposed Rules to audits of all issuers, including EGCs,

[20] See *PCAOB Requests Comment on Engagement Quality Review Standard Under New Post-Implementation Review Program*, PCAOB News Release (Apr. 6, 2016), *available at* http://pcaobus.org/News/Releases/Pages/2016-request-for-comment-AS7-center-post-implementation-review.aspx

[21] While the precise scope of this category of rules under Section 103(a)(3)(C) is not entirely clear, we do not interpret this statutory language as precluding the application of Board rules requiring additional factual information about the engagement partner and certain audit participants to the audits of EGCs. In our view, this approach reflects an appropriate interpretation of the statutory language and is consistent with our understanding of the Congressional purpose underlying this provision.

the PCAOB requested that the Commission make the determination required by Section 103(a)(3)(C). To assist the Commission in making its determination, the PCAOB prepared and submitted to the Commission its own EGC analysis. The PCAOB's EGC analysis includes discussions of characteristics of self-identified EGCs and economic considerations pertaining to audits of EGCs, including efficiency, competition, and capital formation.

In its analysis, the Board states, with support from commenters, that requiring the same disclosures for audits of EGCs as for all issuers would provide the same general benefits to investors in EGCs as would be applicable to investors in non-EGCs. On the cost side, the Board does not believe that compliance costs for auditors will be significant. Rather, based on the overall characteristics of EGCs, the Board believes it is unlikely that the cost of collecting data to comply with the Proposed Rules will be disproportionately high for EGCs as a group. Further, the Board's analysis notes that commenters generally indicated they were not aware of any significant costs that would be specific to audits of EGCs when compared to the costs of non-EGC audits.

The PCAOB's EGC analysis was included in the Commission's public notice soliciting comment on the Proposed Rules. Based on the analysis submitted, we believe the information in the record is sufficient for the Commission to make the requested EGC determination in relation to the Proposed Rules. The Commission also takes note, in particular, of the PCAOB's approach to the Proposed Rules, which are not intended to substantively change auditor performance requirements; should reduce investors' search costs since the information will be provided in one place in a searchable database; and have been developed in a way to mitigate potential increases in auditor liability. In addition, the auditor's requirements under the new standard are focused on communicating the characteristics of the auditor, of which the auditor is

already aware or can readily obtain.

V. Conclusion

The Commission has carefully reviewed and considered the Proposed Rules and the information submitted therewith by the PCAOB, including the PCAOB's EGC analysis, and the comment letters received. In connection with the PCAOB's filing and the Commission's review,

A. The Commission finds that the Proposed Rules are consistent with the requirements of the Sarbanes-Oxley Act and the securities laws and are necessary or appropriate in the public interest or for the protection of investors; and

B. Separately, the Commission finds that the application of the Proposed Rules to EGC audits is necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation.

IT IS THEREFORE ORDERED, pursuant to Section 107 of the Sarbanes-Oxley Act and Section 19(b)(2) of the Exchange Act, that the Proposed Rules (File No. PCAOB-2016-01) be and hereby are approved.

By the Commission.

Brent J. Fields
Secretary

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