

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

August 7, 2023

Re: Amendments to PCAOB Auditing Standards related to a Company’s Noncompliance with Laws and Regulations

Dear Chair Williams,

On behalf of Public Citizen and Americans for Financial Reform Education Fund, we welcome the opportunity to respond to the Public Company Accounting Oversight Board’s request for comment on amendments to AS 2405, *A Company’s Noncompliance with Laws and Regulations*, and AS 2110, *Identifying and Assessing Risks of Material Misstatement*.¹ The fundamental obligation of auditors in reviewing financial statements is to ensure that there are no material misstatements of a company’s financial position. We commend the PCAOB for seeking to clarify and strengthen an auditor’s duties to identify and evaluate information that might indicate a reporting company’s noncompliance with laws or regulations, including fraud, and to make appropriate communications to management and the audit committee about such information.

The climate crisis and the economy-wide decarbonization transition are creating new incentives and opportunities for companies to misrepresent their financial position. To promote a sustainable and resilient financial system, auditors must fulfill their critical role of preventing material misstatements and detecting noncompliance with environmental and social laws and regulations. Auditors serve as a “public watchdog” to reasonably assure the absence of material misstatements and financial fraud.² By directing auditors to identify all applicable laws and regulations—including new corporate disclosure regimes on climate-related financial risks—and to examine more sources of publicly available information on a company’s operations, strategy, and financials, the proposed rule will help auditors detect fraud and noncompliance that give rise to material misstatements in financial reporting. In particular, the PCAOB’s directive that auditors look out for and report to management and the audit committee all potential and confirmed instances of noncompliance with laws and regulations, regardless of perceived materiality on the financial statements, strengthens corporate accountability.

¹ Public Company Accounting Oversight Board (PCAOB). 2023. “Amendments to PCAOB Auditing Standards related to a Company’s Noncompliance with Laws and Regulations”

² *United States v. Arthur Young & Co.*, 465 U.S. 805 (1984)

To build on the PCAOB’s proposed amendments, and with a focus on the material and growing threat of climate change to corporations and their investors, we make the following observations and recommendations:

1. Oil and gas companies to date have exploited Generally Accepted Accounting Principles (GAAP) to keep massive asset retirement obligations (AROs) off their balance sheets and hidden from investors. In 2006, Standard & Poor’s estimated that 50% of European fossil fuel companies’ debt obligations were AROs.³ The PCAOB should amend AS 2110 and AS 2405 to reinforce requirements with an affirmative duty by auditors to investigate and ensure appropriate disclosure of off-balance sheet AROs to address noncompliance and to avoid material misstatements.
2. The PCAOB rightly stresses auditors’ duties to uncover and evaluate environmental remediation liabilities (ERLs) to reasonably assure that companies are in compliance with relevant environmental laws and regulations. The failure to report these liabilities obscures fossil fuel companies’ true financial condition,⁴ and it has led to legal actions against fossil fuel companies in the past.⁵ We commend the PCAOB for including ERLs in the proposal document to ensure auditors are on notice that turning a blind eye to this risk of noncompliance leads to material misstatement.
3. The mismatch between corporate sustainability pledges and business practices is a major source of greenwashing and investor confusion. We agree with the PCAOB that auditors should examine and compare companies’ sustainability disclosures and “net-zero” commitments across different corporate communications channels—including press releases, corporate sustainability reports and SEC filings—to assess the risk of material misstatements in the audited financial statements. In addition, the PCAOB should make clear that net-zero commitments cannot be premised on carbon offsetting, per the standards of global standard-setters such as the SBTi and Voluntary Carbon Markets Initiative, as that would obscure a fair presentation of a company’s decarbonization efforts, corporate strategy, and potentially the financial statements.⁶

³ Carbon Tracker Initiative. 2020. *Flip Side: How Stranded Assets Will Give Rise to Stranded Liabilities*. London: Carbon Tracker.

https://carbontracker.org/wp-content/uploads/2020/02/Decommissioning-Analyst-Note_vwebsite-1.pdf?lang=ja, at 2.

⁴ *Id.*

⁵ National Whistleblower Center. 2020. *Exposing a Ticking Time Bomb: How Fossil Fuel Industry Fraud is Setting Us Up for a Financial Implosion – and What Whistleblowers Can Do About It*. Washington: National Whistleblower Center at 18.

<https://www.whistleblowers.org/wp-content/uploads/2020/07/NWC-Climate-Risk-Disclosure-Report.pdf>

⁶ Greenfield, Patrick. 2023. “Drop carbon offsetting-based environmental claims, companies urged.” *The Guardian*, July 10, 2023, <https://www.theguardian.com/environment/2023/jul/10/carbon-offsetting-environmental-claims-aoe>.

4. As the world tackles the climate crisis and economy-wide decarbonization, it is evident that currently used accounting estimates and assumptions are likely obscuring financial risks and opportunities. The Inflation Reduction Act, for example, has dramatically changed investing fundamentals across the transportation, power, buildings, and industrial sectors. Demand destruction for fossil fuels is ongoing. The PCAOB should underscore that reliance on estimates and assumptions tied to past conditions is no longer an acceptable proxy for the many forward looking estimates and assumptions required, such as remaining useful lives and recoverable values in impairment testing.
5. We agree with the PCAOB that auditors must stay informed of the fast-evolving regulatory environment and consider how changing laws and regulations may impact a company's noncompliance and financial risk, as well as the appropriateness of estimates and assumptions. Auditors can credibly assess compliance only if they are knowledgeable about a company's business and industry, including relevant climate, environmental and financial laws and regulations.

I. Auditors should identify environmental and climate-related noncompliance with laws and regulations.

A. Asset retirement obligations

Asset retirement obligations (AROs) are legal obligations governed by local, state, and federal law associated with the retirement of long-lived assets, such as wells, pipelines, mines, power plants, or other carbon-intensive infrastructure. The most common form of ARO is the legal mandate to plug and abandon (P&A) oil and gas wells upon reaching the end of their productive life. AROs are a significant cost for oil and gas companies. In 2006, Standard & Poor's estimated that 50% of European fossil fuel companies' debt obligations were ERLs and AROs.⁷ Yet these costs are still largely hidden.

Oil and gas companies are legally obligated to decommission tangible assets at the end of their useful life, which is inevitable given policy, consumer, and economic changes in response to the climate emergency. However, many companies, like Valero Energy Corporation, make no provision for AROs by claiming that they have no ability to estimate the retirement timeline of their fossil fuel assets. In Valero's annual report, it claims: "It is our practice and current intent to maintain all our assets and continue making improvements to those assets based on technological advances. As a result, we believe that assets at our refineries and plants have indeterminate lives for purposes of estimating asset retirement obligations because dates or ranges of dates upon which we would retire such assets cannot reasonably be estimated at this time."⁸

⁷ Flip Side, *supra note 3* at 2.

⁸ Valero, 2022. "Form 10-K."

<https://www.sec.gov/ix?doc=/Archives/edgar/data/0001035002/000103500223000027/vlo-20221231.htm>.

Energy companies use spurious claims of indeterminate life to keep massive ARO liabilities off their balance sheets. In fact, most oil and gas companies do not report their decommissioning obligations for midstream and downstream segments like refineries and pipelines due to indeterminate life arguments.⁹ Some auditing firms, such as Deloitte, are starting to signal that the concept of “indeterminate life” should only be used in rare circumstances.¹⁰ As the energy transition accelerates, driven by new laws and regulations, companies will increasingly need to recognize asset retirement obligations previously thought to have indefinite or unrealistically long life spans.

Carbon Tracker estimates that unexpected asset retirements for the seven super oil majors alone (BP, Chevron, ENI, Exxon, Shell, Total, and ConocoPhillips) could cause costs and commitments to soar from a reported \$87 billion (the aggregate cost as currently identified in company filings) to a staggering \$294 billion.¹¹ Many carbon-intensive assets will require earlier retirement than anticipated in previous audited financial statements. If companies are underreporting these obligations, they will undoubtedly face the risk of noncompliance with environmental laws and regulations upon the retirement and decommissioning of carbon-intensive assets. Consequently, auditors will need to accelerate the recognition of decommissioning costs and asset retirement obligations, leading to a sudden increase in reported liabilities.¹² To be in accordance with current accounting and disclosure standards, PCAOB should direct auditors to scrutinize AROs that are often unreasonably—and misleadingly—minimized in statements.

Investors at Exxon have already put forth a shareholder resolution to request a full disclosure of the quantitative impact of off-balance-sheet asset retirement obligations in a net-zero by 2050 scenario.¹³ Investors—and more scrupulous accounting firms—recognize this information is financially material. Unfortunately, a study from the Government Accountability Office determined that without access to company records, it is extremely difficult to evaluate an oil and gas company’s environmental remediation liabilities and asset retirement obligations.¹⁴

⁹ Principles for Responsible Investment. “Report impact of energy transition on asset retirement obligations at Imperial Oil Limited.” New York: PRI. <https://beta.unpri.org/group/16781/stream>

¹⁰ Deloitte, 2022. “Environmental Obligations and Asset Retirement Obligations” at 83. <https://dart.deloitte.com/USDART/pdf/b702f3de-7b0f-11e8-85b9-f5946165e692>

¹¹ Flip Side, *supra* note 3 at 1.

¹² Ross, Samantha. 2021. *The Role of Accounting and Auditing in Addressing Climate Change*. Washington: Center for American Progress, <https://www.americanprogress.org/article/role-accounting-auditing-addressing-climate-change/>.

¹³ Carbon Tracker Initiative. 2023. *Carbon Tracker Initiative’s Response to Exxon’s 14A filing*. London: Carbon Tracker Initiative. <https://carbontracker.org/response-to-exxons-14a-filing/>.

¹⁴ Government Accountability Office (GAO). 2004. “Environmental Disclosure: SEC Should Explore Ways to Improve Tracking and Transparency of Information, United States Government Accountability Office: Report to Congressional Requesters.”

B. Environmental remediation liabilities

Environmental remediation liabilities (ERLs) are contingent liabilities that result from noncompliance with environmental regulations related to contamination in soil, water, and sediment at local, state, federal, or even international levels.¹⁵ The fossil fuel industries' extractive activities result in toxic waste and other environmental impacts that generate liabilities that are rarely disclosed in financial statements.¹⁶ Oil and gas companies frequently fail to disclose their environmental liabilities by using creative accounting to defer and conceal these costs, sometimes indefinitely.

During periods of time when no property transfer or official determination by the government concerning cleanup standards takes place, some corporations delay the assessment of environmental liabilities for their polluted sites. Fossil fuel companies avoid triggering requirements for environmental assessments by engaging in tactics like idling facilities instead of closing, selling, or transferring them, thereby keeping significant environmental liabilities off corporate financial reports.¹⁷ These idle sites, which are often near low-income communities and communities of color, release toxic waste and endanger public health. To combat these practices, auditors should gauge the potential risk of material misstatement by developing an understanding of management's processes for investigating, identifying, and communicating noncompliance with environmental laws and regulations.

Fossil fuel companies have failed to comply with environmental laws and regulations that require disclosing their environmental decommissioning liabilities to remove or remediate pollution or contamination in their financial statements.¹⁸ In 2015, Anadarko Petroleum, which is now owned by Occidental Petroleum, reached a settlement of \$5.15 billion to resolve accusations that Kerr-McGee Corporation (acquired by Anadarko) had sold assets to evade significant environmental liabilities.¹⁹ In addition, the SEC found that Ashland Inc. and William Olin had inappropriately decreased the cost estimates for remediation of environmental contamination at numerous chemical and refinery sites under Ashland's responsibility, leading to an understatement of the company's environmental liabilities.²⁰

¹⁵ Deloitte. 2022. "On the Radar: Environmental Obligations and Asset Retirement Obligations." New York: Deloitte, <https://dart.deloitte.com/USDART/home/publications/deloitte/on-the-radar/environmental-obligations-aro>

¹⁶ Rogers, Greg. 2016. "Accounting for Oil and Gas Environmental Liabilities in Bankruptcy." Eratosthenes. <http://www.era-tos-thenes.com/wp-content/uploads/2016/09/Accounting-for-Environmental-Liabilities-in-Bankruptcy.pdf>

¹⁷ Lewis, Sanford. 2014. "Fooling Investors & Fooling Themselves: How Aggressive Corporate Accounting & Asset Management Tactics Can Lead To Environmental Accounting Fraud." Oakland: The Rose Foundation for Communities and the Environment. <https://rosefdn.org/wp-content/uploads/2014/10/Fooling-Investors-Report.pdf>

¹⁸ The Role of Accounting and Auditing in Addressing Climate Change, *supra note 12*.

¹⁹ Exposing a Ticking Time Bomb, *supra note 5* at 18.

²⁰ Department of Justice (DOJ). 2014. "United States Announces \$5.15 Billion Settlement of Litigation Against Subsidiaries of Anadarko Petroleum Corp. to Remedy Fraudulent Conveyance Designed to Evade Environmental Liabilities"

In North Carolina, growing concerns of Duke Energy Corporation's coal ash ponds contaminating waterways and drinking water prompted communities to pursue legal action over environmental damages due to exposure to hazardous waste. Consequently, Duke Energy company reached a \$1.1 billion settlement agreement to clean up its coal ash ponds, resulting in a net income decreased to \$1.37 billion in 2020 compared to \$3.755 billion in 2019.²¹ Ongoing organizing and litigation for environmental cleanup will inevitably force companies to confront environmental remediation costs that they are neglecting to include in their financial statements.²²

These examples of oil and gas companies' concealment of environmental liabilities underscores the necessity for auditor vigilance to detect noncompliance with environmental laws and regulations. Instead, auditors often rubber stamp companies' misrepresentation of fossil-fuel-related liabilities, and investors remain in the dark over significant and material asset retirement obligations and environmental remediation liabilities. However, auditors have access to company information and can require transparent disclosure of noncompliance with environmental laws and regulations to fairly present a company's financial health.

II. Auditors should assess the risk of material misstatement due to climate-related financial risks.

A. Financial statements fail to integrate companies' sustainability disclosures and net-zero commitments.

The climate crisis, climate mitigation regulations and incentives, and investor demand for climate disclosure and sustainable investing options are creating new incentives and opportunities for companies to represent their business risks, strategy, and financial position differently for various audiences, raising the risk of material misstatements in SEC filings. For example, companies today are making net-zero commitments that they opine on in public statements and corporate sustainability reports, but fail to substantiate in their 10-K's and financial statements. To address this misleading conduct, the PCAOB must charge auditors with an explicit responsibility to look beyond the financial statements to understand the events, conditions, and company activities that might reasonably be expected to have a significant effect on the risk of material misstatement. Auditors should be required to review press releases, earnings calls, company-prepared presentation material for analysts or investors, corporate sustainability reports, the company's website and social media accounts, information publicly disclosed by the company's executive officers about the company, and media reporting about the company to inform their understanding and probe inconsistencies and material misstatements.

²¹ North Carolina Utilities Commission. 2021. *Coal Combustion Residuals Settlement Agreement*. <https://starw1.ncuc.gov/NCUC/ViewFile.aspx?Id=53aa44a2-73e0-4908-8c9e-b7fc1663d5e2>

²² Davis, R., & Franks, D. M. 2014. *Costs of Company-Community Conflict in the Extractive Sector* (Corporate Social Responsibility Initiative Report No. 66). Harvard Kennedy School. http://www.csr.uq.edu.au/media/docs/603/Costs_of_Conflict_Davis-Franks.pdf.

Specifically, the PCAOB should direct auditors to look more closely at the alignment between public climate commitments, decarbonization strategies, and SEC filings. Thousands of public companies have made public commitments to achieve net zero greenhouse gas emissions by 2050—commitments which would often require fundamental change to the company’s strategy and capital expenditures—without substantiating or even mentioning that strategy in their SEC filings.²³ Various public oil and gas companies and financial firms have committed to achieving net zero greenhouse gas emissions by 2050, while their financial statements estimate future cash flows from certain fossil fuel assets and investments based on them having “indefinite lives” with decommissioning “more than 50 years away.”²⁴ Four of the five major standard setters and initiatives currently require a phase out of fossil fuels for net zero transition plans to be certified as credible, and the fifth is updating its criteria currently.²⁵ Put simply, many firms are using public climate-related commitments to attract investors, customers, employees, and to generate positive press, while not attempting to actually achieve those goals, and in many cases privately pursuing opposing strategies.²⁶ Additionally, there is often internal inconsistency within SEC filings between the company’s climate risks and strategy as identified in its 10-K, and the impact of those identified climate risks and strategies on the financial statements.²⁷

B. Accounting estimates and assumptions are obscuring risks due to new climate-related laws and regulations.

Unsound climate-related accounting estimates and assumptions pose a significant risk to the material misstatement of financial statements. Certain line items and valuations of carbon-intensive assets in financial statements are calculated using estimates and assumptions about the future. To determine these estimates and assumptions, companies sometimes use

²³ See E.g., News Release: “Carlyle Sets Net Zero by 2050 and Near-Term Climate Goals for Meaningful, Immediate Action with a Focus on Real Emissions Reductions,” Feb 1, 2022, <https://www.carlyle.com/media-room/news-release-archive/carlyle-sets-net-zero-2050-and-near-term-climate-goals>; *The Carlyle Group Annual Report to the SEC*, published Feb 9, 2023, <https://ir.carlyle.com/static-files/dcea0020-8c53-49b1-826b-ad8f32e64585press+release>

²⁴ Carbon Tracker Initiative. 2021. *Flying Blind: The Glaring Absence of Climate Risks in Financial Reporting*. London: Carbon Tracker Initiative.

<https://carbontracker.org/reports/flying-blind-the-glaring-absence-of-climate-risks-in-financial-reporting/>.

²⁵ Net Zero Tracker, “Net Zero Stocktake 2023,” June 2023.

https://ca1-nzt.edcdn.com/Reports/Net_Zero_Stocktake_2023.pdf?v=1689326892

²⁶ CarbonBrief, “Oil Majors not walking the talk on climate action, study confirms,” Feb 16, 2022.

<https://www.carbonbrief.org/oil-majors-not-walking-the-talk-on-climate-action-study-confirms/>;

Houston Chronicle, “Big Oil companies renege on climate change promises, inviting government regulations,” June 19, 2023.

<https://www.houstonchronicle.com/business/columnists/tomlinson/article/shell-bp-climate-break-promises-18152812.php>;

The Guardian, “Big Oil quietly walks back on climate pledges as global heat records tumble,” July 16, 2023,

<https://www.theguardian.com/us-news/2023/jul/16/big-oil-climate-pledges-extreme-heat-fossil-fuel>.

²⁷ Comments from Americans for Financial Reform Education Fund *et al.* to the Securities and Exchange Commission on proposed rule: *The Enhancement and Standardization of Climate-Related Disclosure for Investors*, June 16, 2022. <https://www.sec.gov/comments/s7-10-22/s71022-20131579-301946.pdf>

backwards looking assessments—historical assumptions of carbon pricing and fossil fuel use that may overestimate future cash flows and underestimate stranded asset risk.²⁸

Fossil fuel companies' overly rosy accounting assumptions and estimates in financial statements fails to reflect the rapidly evolving climate-related regulatory environment. The emergence of new climate-related regulations from agencies like the Environmental Protection Agency, the Department of Transportation, and laws like the Inflation Reduction Act will create new risks of regulatory noncompliance and material misstatements based on unrealistic estimates for future cash flows and asset valuations. Regulatory and economic factors like declining demand for oil and gas, the transition to renewable energy, emissions restrictions, and the phase-out of internal combustion engines are now coupled, making it even more challenging to predict future cash flows accurately.²⁹

In addition, increasing scrutiny of fossil fuel and extractive industries' environmental harms, human rights abuses, and Indigenous land rights violations is leading to litigation and community conflict creating greater political, operational, legal, and reputational risks for companies.³⁰ For example, the Dakota Access Pipeline's (DAPL) final cost exceeded \$12 billion when initial project estimates were \$3.8 billion.³¹ These increased expenses stemming from legal challenges and social unrest are often underestimated or unaccounted for in initial project estimates and assumptions.

In light of this, merely relying on historical cost or conservative models falls short of capturing realistic costs, credit losses, and asset devaluation from the dynamic shifts in climate-related laws and regulations. For example, in 2020, BP wrote off \$17.5 billion in oil and gas assets due to its forecasts of an accelerating transition away from fossil fuels, a material impact to a fossil fuel company's projected valuations.³² By relying on unsound assumptions, oil and gas companies are ignoring transition risk and materially misstating their assets and liabilities, increasing the likelihood of noncompliance with emerging climate-related regulations.

²⁸ Ross, Samantha. 2021. *Lifting the Veil: Investor Expectations for Paris-Aligned Financial Reporting at Oil and Gas Companies*. Boston, MA: Ceres.

<https://www.ceres.org/sites/default/files/reports/2021-05/Ceres%20Lifting%20the%20Veil%20Oil%20and%20Gas%205.18.pdf>, at 20.

²⁹Jenkins, J.D., et al. 2022. *Preliminary Report: The Climate and Energy Impacts of the Inflation Reduction Act of 2022*. Princeton, NJ: REPEAT Project.

https://repeatproject.org/docs/REPEAT_IRA_Preliminary_Report_2022-08-04.pdf. The REPEAT Project estimates that a decrease in U.S. consumption of petroleum products and natural gas could lead to a reduction of roughly 5% in crude oil prices and a decrease of approximately 10-20% in U.S. natural gas prices by 2035.

³⁰ Costs of Company-Community Conflict in the Extractive Sectors, *supra* 30.

³¹ Fredericks, C. F., Meaney, M., Pelosi, N., & Finn, K. R. 2018. *Social cost and material loss: The Dakota Access Pipeline*. First Peoples Worldwide.

https://www.colorado.edu/program/fpw/sites/default/files/attachedfiles/social_cost_and_material_loss_0.pdf

³² Reuters Staff. "BP to write off up to \$17.5 bln after reduced oil price forecast." *Reuters*, June 15, 2020, sec. Integrated Oil & Gas.

<https://www.reuters.com/article/bp-writeoffs/bp-to-write-off-up-to-17-5-bln-after-reduced-oil-price-forecast-idUSL8N2DS0VA>

C. Auditors must have knowledge of matters related to the company’s business and industry—including relevant climate, environmental and financial regulations and laws—to credibly assess noncompliance.

A range of new climate-related laws and regulations have been promulgated in recent years, and auditors must identify the ways that companies may be noncompliant. Public companies already or will soon need to comply with new regulations in the U.S. and abroad regarding:

- climate-related financial accounting³³ and disclosures,³⁴
- anti-greenwashing and consumer protection regulations, guidance, and enforcement efforts from the Federal Trade Commission,³⁵ the Commodity Futures Trading Commission,³⁶ and Consumer Financial Protection Bureau,³⁷
- federal contractor requirements around net zero transition plans,³⁸
- enhanced environmental regulations,³⁹ and

³³ Financial Accounting Standards Board, “FASB Staff Educational Paper: Intersection of Environmental, Social, and Governance Matters with Financial Accounting Standards,” March 19, 2021.

https://www.fasb.org/document/blob?fileName=FASB_Staff_ESG_Educational_Paper_FINAL.pdf

³⁴ See E.g., Securities and Exchange Commission, *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, <https://www.sec.gov/files/rules/proposed/2022/33-11042.pdf>; EU Commission, *Commission Delegated Regulation (EU) supplementing Directive 2013/34/EU of the European Parliament and of the Council as regards sustainability reporting standards*, July 31, 2023.

https://ec.europa.eu/finance/docs/level-2-measures/csrd-delegated-act-2023-5303_en.pdf

³⁵ Federal Trade Commission, Proposed rule: *Guides for the Use of Environmental Marketing Claims*, Feb. 6, 2023.

³⁶ Commodity Futures Trading Commission Press Release: “CFTC Whistleblower Office Issues Alert Seeking Tips Relating to Carbon Markets Misconduct,” June 20, 2023. <https://www.cftc.gov/PressRoom/PressReleases/8723-23>

³⁷ Consumer Financial Protection Bureau, Proposed Rule: *Residential Property Assessed Clean Energy Financing (Regulation Z)*, May 1, 2023.

<https://www.consumerfinance.gov/rules-policy/rules-under-development/residential-property-assessed-clean-energy-financing-regulation-z/>

³⁸ Defense Department, General Services Administration, and National Aeronautics and Space Administration, Proposed Rule: *Federal Acquisition Regulation: Disclosure of Greenhouse Gas Emissions and Climate-Related Financial Risk*, Nov. 14, 2022.

<https://www.federalregister.gov/documents/2022/11/14/2022-24569/federal-acquisition-regulation-disclosure-of-greenhouse-gas-emissions-and-climate-related-financial>

³⁹ See E.g., Environmental Protection Agency, Proposed Rule: *New Source Performance Standards for Greenhouse Gas Emissions From New, Modified, and Reconstructed Fossil Fuel-Fired Electric Generating Units; Emission Guidelines for Greenhouse Gas Emissions From Existing Fossil Fuel-Fired Electric Generating Units; and Repeal of the Affordable Clean Energy Rule*, May 23, 2023.

<https://www.federalregister.gov/documents/2023/05/23/2023-10141/new-source-performance-standards-for-greenhouse-use-gas-emissions-from-new-modified-and-reconstructed>; Department of Transportation, Proposed Rule: *Corporate Average Fuel Economy Standards for Passenger Cars and Light Trucks for Model Years 2027-2032 and Fuel Efficiency Standards for Heavy-Duty Pickup Trucks and Vans for Model Years 2030-2035*. July 28, 2023.

<https://www.nhtsa.gov/sites/nhtsa.gov/files/2023-07/CAFE-2027-2032-HDPUV-2030-2035-NPRM-web-version.pdf>

- climate-related financial firm supervision⁴⁰ and regulation⁴¹ that probes inconsistencies between public climate commitments and internal strategy, among others.

These laws and regulations create new conduct and disclosure requirements, as well as new penalties, which must be incorporated into the context in which auditors assess legal noncompliance and the risk of material misstatements. An audit that does not consider this new regulatory environment risks misunderstanding the actual financial position of and risks to the company.

Of course, auditors must also be on the lookout for legal noncompliance in areas beyond climate and raise these matters to the attention of the audit committee. Prior audits that uncovered wrongdoing but failed to relay the information include the scandal at Wells Fargo where millions of checking and savings accounts were opened for the bank's clients without their consent in order for staff to meet sales quotas. Wells Fargo's auditor KPMG discovered the fake accounts but concluded the activity was insignificant in the scheme of the company's financial statements.⁴² The bank's shareholders and other clients however would say otherwise, as Wells Fargo ultimately ended up paying \$3 billion in fines to the Department of Justice and SEC,⁴³ \$1.7 billion in penalties to the Consumer Financial Protection Bureau (on top of another \$2 billion in redress to customers),⁴⁴ and was subject to an asset cap by the Federal Reserve Board of Governors.⁴⁵ Had auditors at KPMG flagged the discovery of the false accounts earlier, the extent of the damage to the company's reputation and ultimately financial statements could have been addressed earlier.

Similarly, Ernst & Young as external auditors for hedge fund Och-Ziff Capital Management failed to follow up on concerns from an entity of the hedge fund that strongly suspected bribes

⁴⁰ See E.g., Federal Reserve Board of Governors, "Principles for Climate-Related Financial Risk Management for Large Financial Institutions," Dec. 2, 2022,

<https://www.federalreserve.gov/newsevents/pressreleases/files/other20221202b1.pdf>;

⁴¹ Office of the Comptroller of the Currency, the Federal Reserve System, and the Federal Deposit Insurance Corporation, Proposed Rule: *Community Reinvestment Act*, May 5, 2022,

<https://www.federalreserve.gov/consumerscommunities/files/cra-npr-fr-notice-20220505.pdf>.

⁴² Iacone, Amanda. Bloomberg Law. Watergate-era Audit Fraud Rules Face Post-Wells Fargo Revamp. Oct 24, 2022.

<https://news.bloombergtax.com/financial-accounting/watergate-era-audit-fraud-rules-face-post-wells-fargo-revamp>

⁴³ Department of Justice. Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices Involving the Opening of Millions of Accounts without Customer Authorization. Feb 21, 2020.

<https://www.justice.gov/opa/pr/wells-fargo-agrees-pay-3-billion-resolve-criminal-and-civil-investigations-sales-practices>

⁴⁴ Consumer Financial Protection Bureau. CFPB Orders Wells Fargo to Pay \$3.7 Billion for Widespread Mismanagement of Auto Loans, Mortgages, and Deposit Accounts. Dec 20, 2022.

<https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-wells-fargo-to-pay-37-billion-for-widespread-mismanagement-of-auto-loans-mortgages-and-deposit-accounts/>

⁴⁵ Federal Reserve Board of Governors. Responding to widespread consumer abuses and compliance breakdowns by Wells Fargo, Federal Reserve restricts Wells' growth until firm improves governance and controls. Feb 2, 2018.

<https://www.federalreserve.gov/newsevents/pressreleases/enforcement20180202a.htm>

were being paid in violation of the Foreign Corrupt Practices Act.⁴⁶ The significant fallout from the scandal led to the hedge fund being renamed Sculptor Capital Management, outflows of about \$13 billion in assets from the fund, and the price of the stock of the hedge fund declining over 75% since then, before being acquired by another financial institution.⁴⁷

We strongly support these proposals from the PCAOB, and urge expeditious strengthening and finalization. For questions, please contact Alex Martin at alex@ourfinancialsecurity.org, Mekedas Belayneh at mbelayneh@citizen.org, and Clara Vondrich at cvondrich@citizen.org.

Sincerely,

Public Citizen
Americans for Financial Reform Education Fund

⁴⁶ Department of Justice. Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay \$213 Million Criminal Fine. Sep 29, 2016.
<https://www.justice.gov/opa/pr/och-ziff-capital-management-admits-role-africa-bribery-conspiracies-and-agrees-pay-213>

⁴⁷ Dickson, Steve and Burton, Katherine. Bloomberg News. Rithm to Buy Sculptor in Wake of Legal Dispute with Och. Jul 24, 2023.
<https://www.bloomberg.com/news/articles/2023-07-24/rithm-agrees-to-buy-sculptor-in-wake-of-legal-dispute-with-och>