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March 27, 2003

Public Company Accounting Oversight Board  
Attention: Office of the Secretary  
1666 K Street, NW  
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 001

Dear Board Members:

We appreciate the opportunity to offer comment to the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") regarding its Proposal of Registration System for Public Accounting Firms and related proposed Rules and Proposed Form 1 (Rulemaking Docket Matter No. 001) that are being considered by the Board for adoption and submission to the Securities and Exchange Commission (the "Commission" or the "SEC").

As the national organization of all U.S. state accountancy regulators, the National Association of State Boards of Accountancy (NASBA) applauds the Board's efforts to implement promptly the requirements of the Sarbanes-Oxley Act of 2002 (the "Act") that are entrusted to the Board. NASBA's member boards (sometimes called the "State Boards") are composed of both licensees and public members. As rule makers themselves, NASBA's constituent boards appreciate the challenges of a politically-charged legislative mandate to shape a transparent, efficient and vigorous regulatory approach to enhancing investor confidence in financial reporting for SEC issuers. As enforcers who remain the only authorities empowered to grant or revoke licenses of CPAs (certified public accountants), NASBA's member boards understand the delicate balance between the need for swift discipline and the necessity of procedural fairness. Finally, as independent government agencies that must operate exclusively on licensing fees, NASBA's member boards are sensitive to budgetary realities that inevitably limit program prerogatives.

NASBA's ongoing primary focus is upon rules and policies relating to enforcement, with special attention to facilitating federal/state cooperation.

#### **I. General Comments About PCAOB Rulemaking.**

In general, NASBA urges that these and other new regulations promote vertical clarity so that state accountancy boards can easily translate PCAOB and SEC case results into swift, equitable and defensible disciplinary actions against audit firms and individual licensees implicated in violations. In so doing, the PCAOB and the SEC will be able to place greater practical reliance upon an effectively administered State Board licensing function that puts the offending licensees

at risk of losing not just their SEC clients but their certificates and their livelihoods as CPAs. We note that state accountancy regulation is not self-regulation by accountants, but licensing and discipline by government agencies based on state law. State Board enforcement can result in discipline in a number of forms, including censure, civil penalties, and revocation of the right to practice and call oneself a CPA. State Boards generally also have the statutory authority to initiate civil actions for injunctions as well as criminal prosecutions against individuals and firms engaged in the unlicensed practice of public accountancy.

We believe that close cooperation and working partnership of the PCAOB and the SEC with NASBA and the State Boards would result in more potent regulatory efforts

## **II. Comments on Selected Provisions of the Proposed Rules and Proposed Form 1.**

**General Note.** To strengthen federal/state coordination of oversight of accountants that do audit work for SEC issuers, we offer a few general thoughts to clarify the role of the State Boards and to reduce the risk of confusion or misunderstanding by accountants or others who may seek to rely upon the PCAOB Rules. In the states (and other U.S. jurisdictions) generally an accountant must meet rigorous standards (including education, experience and examination) to be licensed and thus able lawfully to practice most forms of public accountancy, especially audits and reviews. Such licensed accountants (including certified public accountants or CPAs, as well as – in some States – Licensed Public Accountants) frequently are called “licensees.” Other accountants, called “non-licensees” or “unlicensed accountants,” are not authorized to conduct the practice of public accountancy for which license is required by the applicable state (or other U.S. jurisdiction).

We recognize that in connection with PCAOB oversight of public accounting firms that do audit work for SEC issuers, the PCAOB will seek information about accountants associated with those firms – whether CPAs licensed by State Boards or other accountants. Presumably the other (non-CPA) accountants would include “non-licensees” in U.S. jurisdictions, accountants licensed by other authorities in non-U.S. jurisdictions and, if applicable, unlicensed accountants in non-U.S. jurisdictions. We also recognize that in trying to elicit information about appropriate associated persons, the PCAOB may wish to define that class of persons broadly, as in the proposed definition of “accountant” in the proposed Rules. However, to strengthen NASBA/State Board coordination with PCAOB/SEC oversight, we believe it is very important that the PCAOB Rules recognize the distinct category of accountants licensed by the State Boards – the CPAs (and, also, in some States, Licensed Public Accountants). Presumably analogous considerations may be of interest to non-U.S. licensing authorities with respect to accountants licensed within their respective jurisdictions.

**Proposed Rule 1000. Application of Rules.** NASBA suggests that the wording of this Rule be modified to clarify its intent that the Rules of the Board apply to public accounting firms that are required to register with the Board or that otherwise apply for registration with the Board (for example, in contemplation of seeking audit work for SEC issuers) and not to other public accounting firms (e.g., firms that do no work for SEC issuers and do not apply for registration). As modified, Rule 1000 could read: “The provisions of the Rules apply, according to their

terms, to all public accounting firms that are required by the Rules to be registered with the Board or that otherwise apply for registration with the Board, to all persons associated with registered public accounting firms, and to all associated entities of registered public accounting firms” (proposed revision underlined).

### **Proposed Rule 1001. Definition of Terms Employed in Rules.**

General Comment About Definitions. Regarding definitions generally, NASBA suggests: when terms are defined elsewhere for general use (more than for a particular purpose), whether by the Act, securities statutes or regulations, state law or state licensing authority or by customary use, that those *same* terms generally not be given a substantially *different meaning* from their common use. If the Rules do provide a diverse meaning, in an appropriate case it may be helpful to coin another term to avoid potential confusion. An example is the definition of “accountant” discussed below.

Definition of “Accountant”. In some respects the proposed definition of “accountant” may be viewed as going beyond common usage and thus could lead to misunderstanding. Of concern, there could arise a misperception by the public that accountants do not need to be licensed to do audits or other public accounting since they have been included in an application for registration with the PCAOB. Additionally, without clarification, the official use of the term “accountant” in this context might have the unintended consequence of discouraging individual licensure, thus reducing State Board’s ability to directly discipline wrongdoers. In light of the express requirement of Section 102(b)(2)(E) of the Act that an application for registration shall include “a list of all accountants associated with the firm who participate in or contribute to the preparation of audit reports,” perhaps these potential problems may be attenuated by using a different term, such as “licensed or unlicensed accountant” or “firm accounting professional.”

Add a definition of “appropriate State regulatory authority” based on the definition in the Act: “The term ‘appropriate State regulatory authority’ means the State agency or other State authority responsible for the licensure or other regulation of the practice of accounting in the State or States having jurisdiction over a public accounting firm or associated person thereof, with respect to the matter in question.”

Add a definition of “State” based on the definition in the Act: “The term ‘State’ means any State of the United States, the District of Columbia, Guam, Puerto Rico, the Virgin Islands, or any other territory or possession of the United States.” (Assuming that this change is made, references to “state” would be changed to “State” as appropriate.)

**Proposed Rule 2100. Registration Requirement for Public Accounting Firms.** NASBA concurs that the registration requirement should apply to foreign public accounting firms. Uniformity of protection of investors in the U.S. securities markets requires that the Board have oversight of each public accounting firm that prepares or issues an audit report or plays a substantial role in the preparation or furnishing of an audit report with respect to an SEC issuer. It may be useful to add a sentence to the effect, “A public accounting firm that is not required to

be registered with the Board may register with the Board if it meets applicable requirements.” This would expressly acknowledge that a public accounting firm that does not currently do audit work for an SEC issuer may register in contemplation of seeking that type of work.

**Proposed Rule 2105(a). Action on Applications for Registration – Standard for Approval.** NASBA urges that there be added to the standards for approval of an application for registration an express requirement regarding licensing of the public accounting firm. We suggest something to the effect:

“Absent an exception for a particular applicant in the discretion of the Board (based upon substantial evidence that the exception is justified and fully consistent with the other standards for approval of an application), the application for registration of a public accounting firm shall not be approved unless the firm demonstrates that:

(1) it is duly licensed, registered or permitted in good standing under the laws of each applicable State [defined as suggested above] and each other applicable jurisdiction where or with respect to which the activities of the accounting firm require the accounting firm to be licensed, registered or permitted under the laws of the State or other jurisdiction or the rules, regulations or policies of the appropriate State regulatory authority or other jurisdictional regulatory authority; and

(2) it meets any other requirements of the Commission for recognition of the accounting firm by the Commission, including those set forth in Regulation S-X of the Commission, as it may be amended from time to time.”

**Proposed Rule 2300. Public Availability of Information Submitted to the Board; Confidential Treatment Requests.** In Section (h), we request that the second sentence be revised to provide, “The granting of confidential treatment will not, however, limit the ability of the Board (1) to provide the information as to which confidential treatment was granted to the Commission or to each appropriate State regulatory authority, or (2) to comply with any subpoena validly issued by a court or other body of competent jurisdiction” (proposed revision underlined). [The definition of “appropriate State regulatory authority” would be added as noted above, based on the definition in the Act.] In making this revision, the Board might want to preserve similar flexibility for its cooperation with foreign regulatory authorities, so that the added language might be, “. . . or to each appropriate State regulatory authority or other jurisdictional regulatory authority. . .” The State Boards would want to have available all of the PCAOB’s registration information.

**Proposed Form 1 – Part I – Identity of the Applicant.** In Item 1.7, Applicant’s Licenses, NASBA agrees with the proposed requirement to list “every license or certification number issued to the applicant authorizing it to engage in the business of auditing or accounting” and to “furnish the name of the issuing state, agency, board or other authority” for “each such license or certification number.” NASBA suggests that the reference to issuers of licenses be revised to read, “furnish the name of the issuing State agency, board or other State or foreign licensing authority” (proposed revision underlined). NASBA suggests that there be added a requirement to provide such information for each *associated entity* of the applicant listed in Item 1.6 -- at

least with respect to that *associated entity* engaging in the practice of public accounting in the U.S. or preparing or issuing, or participating in or contributing to the preparation of, *audit reports for issuers*. Likewise, in Item 1.8, Required Licenses and Certifications, NASBA agrees with the proposed requirements and suggests that they be revised to read as follows: “Indicate whether the applicant, each associated entity required to be listed in Item 1.6 and all individual *accountants* associated with the applicant required to be listed in Part VII who participate in or contribute to the preparation of *audit reports for issuers* or comparable reports prepared for clients that are not issuers have in good standing all licenses and certifications and valid practice privileges required by governmental (federal, State and non-U.S.) and, if applicable, professional organizations, and identify by name any such associated entity and any such individual accountant that does not” (proposed revisions underlined). These provisions, especially as proposed to be revised, would help facilitate the coordination of federal and State regulatory efforts. Finally, NASBA suggests that unless there are any licenses, certifications or practice privileges required uniquely by any private professional organizations (i.e., that are not otherwise required in the first instance by governmental (federal, State and non-U.S.) organizations), it likely would be appropriate to delete the reference to professional organizations.

**Proposed Form 1 – Part VII – Roster of Associated Accountants.** In Item 7.1, Listing of *Accountants* Associated with Domestic Applicants, and Item 7.2, Listing of *Accountants* Associated with Non-U.S. Applicants, NASBA strongly agrees with the information listing requirements. Again, these provisions would help facilitate the coordination of federal and state regulatory efforts. Also, NASBA suggests that the last two sentences of Item 7.1 be revised to read: “For each such person, list every license or certification number (if any) and any valid practice privileges authorizing him or her to engage in the business of auditing or accounting. For each such license or certification number, furnish the name of the issuing State agency, board or other State or foreign licensing authority” (proposed revision underlined). Finally, NASBA suggests that the last two sentences of Item 7.2 be revised to read: “For each such person, list every license or certification number (if any) and any valid practice privileges authorizing him or her to engage in the business of auditing or accounting. For each such license or certification number, furnish the name of the issuing State agency, board or other State or foreign licensing authority” (proposed revision underlined).

In Item 7.3, Number of Firm Personnel, part (b) calls for the number of certified public accountants “or *accountants* with comparable licenses from non-U.S. jurisdictions” that are associated with the applicant. We wonder who determines what are “comparable licenses” and how that determination will be made. NASBA hopes to participate in discussions with PCAOB representatives regarding this point.

**Proposed Form 1 – Part IX – Signature of Applicant.** NASBA suggests adding a provision – whether in this part or elsewhere in the Form or the Rules – to the effect that the continuing effectiveness of a registration of a firm with the PCAOB is conditioned, in the discretion of the PCAOB, upon the application being complete in all material respects and not containing any untrue statement of a material fact or omitting to state a material fact necessary to make the

statements made, in light of the circumstances under which such statements were made, not misleading.

### **Drafting Comments.**

The following comments are offered for consideration as drafting matters, to conform certain references, to clarify intended meaning or to amplify proposed provisions consistent with their apparent general intent.

Proposed Form 1 – Item 5.1(a) [criminal actions in connection with *audit reports*]. Consider revising the clause in the middle of the first sentence to read, “. . . is a defendant in any pending criminal proceeding (including a non-U.S. jurisdiction), or was a defendant in any such proceeding . . .” (proposed change underlined).

Proposed Form 1 – Item 5.1(b)(4) [criminal actions in connection with *audit reports*] and various other places. Consider revising this sentence to read, “The name of the *issuer* or other client that was the subject of the *audit report* or other comparable report” (proposed change underlined). This would conform with the reference in 5.1(a) and the definition of audit report. This change appears similarly appropriate in Items 5.2(b)(4), 5.3(b)(4), and 5.4(b)(4).

Proposed Form 1 – Item 5.3(a) [regarding private civil actions in connection with *audit reports*]. Consider adding reference to proceedings initiated by “other persons”. Consider adding reference to alternative dispute resolution proceedings. Consider express reference to “(including a non-U.S. jurisdiction)”.

Proposed Form 1 – Item 5.5(b) [regarding other proceedings]. Consider adding reference to a time period, such as “was, in the previous \_\_\_ years, censured or fined . . .” (proposed change underlined). This would be parallel to the approach in Item 5.5(a).

### **III. Prospective Future Rulemaking by the PCAOB or the Commission.**

NASBA urges that care be taken by the PCAOB and the Commission in drafting these and other regulations so as not to dilute the existing requirement for Commission recognition that a certified public accountant be "duly registered and in good standing as such under the laws of the place of his residence or principal office" and that a public accountant be "in good standing and entitled to practice as such under the laws of the place of his residence or principal office." [Rule 2-01(a) of Regulation S-X; 17 CFR 210.2-01(a)] The current license status of all accountants should be regularly checked with State Boards.

NASBA urges that the PCAOB encourage the Commission to add to the requirements of Regulation S-X regarding "Qualifications of Accountants" a requirement for Commission recognition [and/or that the PCAOB itself require] that an accountant and an accounting firm be duly licensed, registered or permitted or otherwise hold valid practice privileges and be in good standing under the laws of each applicable State (to be defined as suggested above) and each other applicable jurisdiction where or with respect to which the activities of the accountant or the accounting firm require the accountant or the accounting firm to be licensed, registered or permitted or otherwise hold valid practice privileges under the laws of the State or other jurisdiction or the rules, regulations or policies of the appropriate State regulatory authority or other jurisdictional regulatory authority.

Footnote 11 in the PCAOB's Release No. 2003-1 states the acts that restrict US government agencies' disclosure of information do not apply to the PCAOB. However, it is anticipated that the states' privacy laws would be respected by the PCAOB.

**Conclusion.** NASBA appreciates the opportunity to provide these comments. Should you have questions concerning our thoughts on the proposed Rules or other matters, please contact us. We look forward to responding to other proposals as appropriate and to ongoing cooperation and communication with the PCAOB and the Commission.

Sincerely,



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Chair, NASBA



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