AMERICAN BAR ASSOCIATION
Section of Business Law
750 North Lake Shore Drive
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August 21, 2003

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

Re: Rulemaking Docket Matter No. 005

Ladies & Gentlemen:

On behalf of the Committees on Law & Accounting and Federal Regulation of Securities of the Section of Business Law of the American Bar Association (the "Committees"), we are writing to express our views with respect to the Release No. 2003-012 of the Public Company Accounting Oversight Board (the "Board" or "PCAOB") in which the Board has proposed rules for the conduct of investigations and hearings. The views expressed herein are those of the Committees and have not been approved by the Section of Business Law or the House of Delegates or Board of Governors of the American Bar Association ("ABA"). Accordingly, they should not be construed as representing the policy of the ABA. This letter was drafted by a task force composed of members of the Committees whose names are set forth below, and the Committee Chairs and members of the task force are available to discuss the matters discussed herein with the Board and its staff.

General Comments

We would like to begin our comments by commending the Board and its staff for assembling a comprehensive and generally well-conceived set of rules for the conduct of investigations and hearings in the very limited period necessitated by the timetable prescribed by Congress in the Sarbanes-Oxley Act of 2002 (the "Act"). The proposed rules generally reflect a careful balancing of the need to protect the public and the rights of accounting practitioners whose lives and livelihoods will be greatly affected by the Board's actions arising out of its investigations and disciplinary hearings.

We appreciate that (a) the Board is acting on time constraints imposed by Congress in the Act, (b) many of its proposed rules are closely modeled after the Rules of Practice of the Securities and Exchange Commission (the "Commission" or "SEC"), and (c) those wishing to comment on the Board's proposals will have an additional opportunity to do so when they are again released for public comment by the Commission. Nevertheless, in view of the length and complexity of the proposed rules, their importance to the members of the accounting profession who audit public companies as well as to issuers, and the Board's simultaneous publication of proposed rules relating to firm inspections and firm withdrawals from registration, a three-week

comment period has not provided sufficient time for a thorough review and discussion of the proposal by our members.

Because of the severe time constraints imposed by the limited comment period, our comments are largely focused on the issues that are addressed in the proposed rules. We have not had a full opportunity to consider those matters which might have been included in the proposed rules but have been omitted either by design or oversight.

For the sake of simplicity and ease of review, we have organized our comments based upon the order in which the subjects are addressed in the proposed rules, and not on the basis of their relative importance. Many of our comments are addressed to minor matters; we have proceeded on the basis that now is the appropriate time to correct minor mistakes.

Specific Comments

Rule 1001(h)(i). This rule includes within the definition of "hearing officer" one or more members of the Board so long as they constitute less than a quorum of the Board. We question the wisdom of having Board members serve as hearing officers as we do not believe that this would be a good use of their time, especially since hearings often can consume many full days. More importantly, serving as a hearing officer would disqualify any such Board member from reviewing the findings of the hearing officer, posing the potential problem of obtaining a quorum of Board members to consider an appeal from a ruling of the hearing officer. It should also be pointed out that under Rule 5200(b) hearing officers are appointed by the Secretary and it seems wholly inappropriate for the Secretary to have the power to appoint a member of the Board.

We are also concerned that the rule proposal would allow "any other person duly authorized by the Board" to serve as a hearing officer. There clearly are certain attributes that a hearing officer must have – lack of bias, judicial temperament, an understanding of relevant regulatory requirements, and so on. We would urge the Board to establish hearing officer positions within the Board staff, much like the role served by the SEC's Administrative Law Judges. These professional hearing officers would have the necessary attributes so that the public and the profession can have full confidence in the integrity of the administrative process.

Rules 5102(b)(3) and 5105(a)(1). These provisions require that the Board's staff include a description of the subject matter of the testimony in a demand for testimony only in the case of testimony of a "registered public accounting firm." We see no reason why the requirement for the subject matter of the testimony should not also apply to demands served on persons associated with a registered public accounting firm. This appears to be a drafting oversight.

Rule 5102(c)(3). This rule limits the persons allowed to be present during the taking of investigative testimony and provides that the witness may only be represented by legal counsel. Since the subject matter of the Board's investigations are likely to involve technical accounting issues, as to which legal counsel may lack appropriate understanding, we believe that adequate representation may only be achieved by allowing legal counsel to be assisted by an accounting expert.

Rule 5102(e). This rule requires a witness to request changes to the transcript of his or her testimony given in a Board investigation within 10 days of being notified that the transcript is available. This seems to be an unnecessarily short period of time, and we recommend that the period be extended to at least 30 days.

Rule 5105(a)(2). In referring to the individual to be examined on behalf of a person that is an entity, this rule refers to the designated individual as a "person." This implies that an entity can designate another entity to testify on its behalf. We suggest that the "designated person" be referred to as an "individual."

Rule 5106. This rule addresses the assertion of privilege in an investigatory proceeding and requires the respondent to provide a host of information in order to assert a privilege. Some of that information will not always be readily available. We, therefore, believe that a certain amount of flexibility must be drafted into this provision. We also are concerned that the failure to provide the required information would place the respondent in the uncomfortable position of either having to waive a privilege or risk being cited for non-cooperation with the Board's investigation.

Rule 5109(a). This rule permits the Director of Enforcement and Investigations to honor a respondent's requests for a copy of a formal order of investigation. We strongly believe that respondents should have this right and believe that it should not be a matter of discretion. If necessary, the Board's rules should require the requesting party to agree to certain limitations upon his or her use of the order.

Rule 5109(d). This rule affords a respondent in an investigation the opportunity to submit a "statement of position" to the Board in defense of his or her actions which are the subject of a possible request by the staff to initiate a disciplinary proceeding. Such a statement corresponds to a "Wells submission" in an SEC investigation. The rule, however, provides the staff with "discretion" as to whether it wishes to advise the respondent of the nature of its proposed allegations. We believe that such discretion defeats the purpose of a procedure that in SEC administrative practice has proven helpful in focusing the issues in dispute. Accordingly, we recommend that the staff not only be required to provide the respondent with information concerning its proposed charges, but also that the information identify all professional and regulatory provisions alleged to have been violated as well as the specific actions of the respondent that are the basis for the allegations.

Rule 5110. This provision authorizes the Director of Enforcement and Investigations to recommend to the Board that a disciplinary proceeding be instituted where a firm or associated person may have given false or misleading testimony or testimony that omits material information. We are troubled by this standard as we strongly believe that in any such circumstances the burden should be on the Board to establish that the question that was not properly addressed specifically requested the omitted information and that the omission was not inadvertent.

Rule 5200(a)(2). Under this provision, the Board has the power to commence a disciplinary proceeding against "supervisory personnel" for having failed to supervise an

associated person. Unfortunately, the term "supervisory personnel" is not defined in the Act or in the Board's rules and conceivably could cover a senior accountant performing field work with junior accountants. We recognize that in any audit engagement, there is a chain of command; however, we do not believe that all persons within that chain properly could be viewed as "supervisory personnel." Instead, we would limit supervisory responsibility to the partner in charge of the audit and the audit manager. Concurring partners, engagement partners and review partners, while fulfilling important roles, should not be burdened with supervisory responsibility. Similarly, we have concerns as to what constitutes a failure of "reasonable supervision." We believe that it will be necessary for the Board to spell out this new requirement in its rules because we are not aware of any body of professional literature discussing it.

Rule 5200(b). This rule enumerates the powers of the hearing officer. Absent from the list of such powers are the powers to resolve disputes relating to documentary disclosures. We also suggest the inclusion of an additional power to perform all other duties authorized elsewhere in the rules.

Rule 5201(a). The rule, which provides for notice of the commencement of a disciplinary proceeding, is silent as to the amount of notice that is required before the first hearing date. Considering the fact that the respondent will only have access to the investigatory files accumulated by the staff after the order initiated the hearing has been issued, hearings should not be permitted to commence until at least ninety days after such notice so as to provide the respondent a reasonable time in which to prepare his or her defense.

Rule 5201(b). This rule, which specifies the content of an order instituting proceedings, does not provide that the order would set the hearing date with respect to disciplinary proceedings under Rules 5200(a)(1) and (a)(2) but would set the hearing date with respect to proceedings pursuant to Rule 5200(a)(3). This may have been an oversight, or it may have been intended that the hearing officer would be given the power to set hearing dates, which would perhaps be a more logical means of setting hearings dates. We note, however, that in the list of powers provided to hearing officers in Rule 5200(b) no reference is made to the power to set hearing dates.

Rule 5204(a). In the third from last line the final "e" should be deleted from the word "therefore."

Rule 5301(a). In the note following this rule, it is stated that a person who is barred or suspended from being associated with a registered public accounting firm "may not in connection with the preparation or issuance of any audit report, (i) share in the profits of, or receive compensation in any other form from, any registered accounting firm, or (ii) participate as agent on behalf of such firm in any activity of that firm." This note is confusing in view of the fact that the Board or the Commission has the power to consent to the individual's continued employment by the firm. If a partner of a registered firm is barred, does that mean that the firm cannot return the partner's capital or pay that partner a separation payment as provided in the firm's partnership agreement? Similarly, if the barred employee is allowed to remain with the firm so long as he does not become involved with public company clients, may the firm pay him

or her a salary or other compensation not related to the firm's public company practice? We believe that the rules must address such questions.

Rule 5302. This rule provides that a person who has been subjected to a Board sanction may apply for the termination of "any continuing sanction" and the applicant may, in the Board's discretion, be afforded a hearing. While we believe that this is altogether appropriate, there are no provisions in the rules governing any such hearings. This appears to be an oversight.

Moreover, the form of petition for termination of ongoing sanctions imposes upon the applicant the burden of providing information that may not be readily available to him, such as the disciplinary history of other persons associated with the same registered public accounting firm. Such information is probably more readily available to the Board and is not particularly relevant to whether the individual may safely be employed by the firm.

Rule 5401(b). As noted earlier in this letter, we believe that fair representation of a respondent in a disciplinary hearing may require respondent's counsel to be assisted by an accounting expert. Although we assume that this provision was not intended to negate that possibility, we believe the Board should make this point explicitly.

Rule 5401(c). This rule raises the question of what is "practice before the Board" and the Board's power to regulate such persons, a subject which is not addressed in these rules. This has proven to be a troublesome issue in practice before the Commission, and we believe that it should be addressed in the Board's rules, although not necessarily in its rules relating to investigations and disciplinary proceedings.

This rule also raises the question of when an individual acting in a representative capacity may withdraw from a Board proceeding. We suggest that the rule be revised to provide that the Board, at the very least, may not unreasonably withhold its permission for such an individual to withdraw. We also have concerns that it may have the effect of requiring a respondent to continue with a legal representative in whom he has lost confidence. Thus, any request by the represented party should be honored in all cases.

Rule 5402(a). Under this rule, a motion for a hearing officer to recuse himself or herself is to be addressed to the hearing officer in the first instance. Such motions should be subject to an interlocutory appeal, with the Board having an offsetting power to impose fines for appeals that are deemed to be frivolous.

Rule 5402(b). When a replacement hearing officer has been appointed, we believe that the parties should have the right to move that certain testimony be reheard so that the replacement hearing officer can better judge the credibility of the witness. We do not disagree that the decision as to whether such rehearing is necessary should remain with the new hearing officer, whose decision thereon would be subject to Board review.

Rule 5408. The time and page limitations relating to motions appear to be unduly restrictive and assume that all motions to be presented to a hearing officer will be of a discreet nature. Moreover, whereas the hearing officer has the power to expand the page limitation, there

is no corresponding power with respect to extending the response period. We presume that this is an oversight.

Rule 5422. This rule specifies the documents that the staff must make available to the respondents. Although the scope of the documents required to be disclosed appears to be appropriate, there is no specification as to when the disclosure is to take place or how the copying is to be effected. Similarly, while subsection (e) specifies that the copying is to be at the respondent's expense, there is no attempt to state what the cost would be if the copying is to be effected by the Board. Does this mean that the respondent has the right to select a copying service to make the copies?

Rule 5424(a)(4). This rule provides that a non-party witness who is summoned to a hearing or deposition shall be reimbursed for his or her "reasonable expenses." Who is to make this determination and what are the criteria of "reasonableness." Does "expense" include hourly wages or charges?

Rule 5425(a). This rule would appear to limit the use of depositions solely to preserve testimony and not for discovery purposes. This places the respondent at a distinct disadvantage as the staff has virtually unlimited power to take testimony during the discovery period. Thus, the respondent is forced to ask questions of a witness at his peril during the hearing, not knowing in advance how the witness will testify. Under such circumstances, respondents might be reluctant to pursue questions that could be beneficial to their position. Moreover, it is not even clear when such a deposition can be taken as the rules do not address the criteria to be used by the hearing officer in setting the dates of the hearings. We, therefore, believe that in view of the dire consequences that could befall a professional in a Board disciplinary hearing, the rules should provide for discovery beyond that provided by the staff.

Rule 5425(d). This provision, which relates to the conduct of depositions, refers to a "deposition officer." Unfortunately, the rules do not address the qualifications or appointment or duties of this individual. We presume that this is simply an oversight.

Rule 5441. In our view, this section highlights the brevity in the proposed rules of any description of evidentiary rules that might apply to a Board hearing. Although it is explained in the "section-by-section analysis" that this is intended to afford the hearing officer flexibility in conducting the hearing, such flexibility does little to assure uniformity of practice or fairness when the hearing officer is employed by the prosecuting agency. Moreover, the criteria for excluding evidence does not include the prejudicial nature of the evidence, its competence or authenticity. While, as lawyers, we appreciate the potential complexity of evidentiary rules, we are concerned that the broad range of discretion provided to the hearing officer is inappropriate in disciplinary proceedings which have the power to preclude a professional from being able to continue practicing which is being decided by an employee of the Board. We, therefore, urge the Board to adopt greater structure for evidentiary rulings.

Other Comments

Missing from the proposed rules is a statement as to who has the burden of proof in a disciplinary hearing and the degree of that burden (i.e., "by a preponderance of the evidence", etc.). Under what circumstances would the burden shift?

It is also not clear what standard can be the basis of a disciplinary proceeding. For example, can a registered person be subjected to a disciplinary proceeding for a single act of negligence? This was an issue faced by the Commission in the *Checkosky* decisions, and it behooves the Board to address this issue and avoid protracted litigation on the subject. Sanctions are discussed in Rule 5300 which is silent on this point.

We hope that these comments will be of assistance in finalizing its rules with respect to the conduct of investigations and hearings. Members of our committees are available to discuss these and other comments. If you believe that such discussions would be helpful, please contact either of the undersigned.

Respectfully submitted,

Committee on Law & Accounting

/s/ Thomas L. Riesenberg

by Thomas L. Riesenberg,
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