

# Professional Oversight Board

Aldwych House, 71-91 Aldwych, London WC2B 4HN

Telephone: 020 7492 2341 Fax: 020 7492 2359

[www.frc.org.uk/pob](http://www.frc.org.uk/pob)

Mark Olson,  
Chairman,  
PCAOB,  
1666 K Street,  
N.W.,  
Washington,  
D. C. 20006-2803.

2 February 2009

Dear Mark

## **PCAOB Rulemaking Docket Matter No. 027 – Release 2008-007**

I am pleased to respond on behalf of the UK's Professional Oversight Board of the Financial Reporting Council to your request for comments on the proposed rule amendment and other issues related to PCAOB inspections of non-US firms raised in Release No. 2008-007.

The Board continues to believe in the importance of effective co-operation between audit regulators internationally in discharging our respective regulatory responsibilities and, in that context, welcomes the opportunity to provide you with our views.

Our principal comments are set out below. We respond to the specific matters on which views were invited in the Appendix to this letter.

### **Importance of moving towards a full reliance approach**

We wish to reiterate the importance we attach to the PCAOB moving towards placing full reliance on the work of independent audit regulators in other jurisdictions, as soon as possible, in particular where the PCAOB already has had the opportunity to work with the independent regulator and gain confidence in their work. A system of reliance on other independent regulators' work with effective two way communication is likely to be the most efficient way of achieving our mutual objective of safeguarding audit quality. Such a system would avoid the significant unnecessary duplication of regulatory effort that currently exists and would promote a cost effective system of regulation which best serves the interests of our respective stakeholders. There are a number of comments in the Release that

would seem to support this view. We consider that this now needs to be followed through into the specific proposals. Such an approach should reduce significantly the practical problems faced by the PCAOB in conducting inspections of non-US firms. Accordingly any proposals aimed at addressing the challenges of inspecting non-US registered firms should be taken forward together with substantive proposals for moving towards a full reliance approach as envisaged by your consultation on Rule 4012 and comments received thereon.

### **Scope of consultation**

We note that the Release focuses primarily on first inspections of non-US firms. In so doing the proposals treat those non-US firms who have already been subject to inspection either directly by the PCAOB or jointly with the local regulator less fairly than those who have not. In particular we consider that it would be wrong in principle, and unfair, for the PCAOB to try to press ahead with 2009 second inspections of a firm which because of legal restrictions, was unable to cooperate fully on a second 2009 inspection. This could lead, on the PCAOB's current proposals, to the imposition of sanctions on such a firm, even where the firm's independent national regulator (with whom the PCAOB had already worked), could provide the PCAOB with the outcome of its independent inspection. We strongly believe that stakeholder interests would be best served were the PCAOB to direct its resources towards non-US firms who had not previously been inspected, and/or where detailed information was not available to the PCAOB on the outcome of independent inspection from that firm's national regulator.

### **European statutory audit directive**

As you aware the European statutory audit directive contains provisions aimed at facilitating the effective sharing of information between regulators within a confidential framework. The implementation of these arrangements requires a decision to be taken in Europe on the adequacy of the PCAOB's arrangements for maintaining confidentiality and will require reciprocal information sharing provisions. From a UK perspective, an adequacy decision and reciprocal arrangements will be necessary before further PCAOB inspections can be freely conducted in the UK. We believe that transitional arrangements similar to those offered in relation to first time inspections should be extended to all firms whilst appropriate adequacy decisions are taken and reciprocal arrangements established.

### **Sanctions**

Where further inspections of firms in a particular jurisdiction are not possible due to legal provisions, the PCAOB should be able to obtain appropriate comfort regarding the competence of the local regulator and the rigour of its work from its experience of working with the local regulator in conducting previous inspections. If, in this

situation, the local regulator is able to provide the PCAOB with a report on a recent inspection undertaken by it of a firm for which a PCAOB inspection has become due, no sanctions should be placed on the firm concerned due solely to the firm's inability to participate in an inspection involving the PCAOB.

### **Transparency proposals**

As a principle the Professional Oversight Board supports transparency proposals aimed at improving investor confidence in audit quality. However, we are concerned that the PCAOB's current proposals may have the unintended consequence of reducing investor confidence inappropriately. Investors may incorrectly conclude that any firm included on the list of firms with a delayed PCAOB inspection is not subject to independent inspection and may have weak or inadequate quality control procedures. If it is deemed necessary to make any disclosure of such firms, then the disclosure should make clear the reasons for the delay, the extent to which the firm has been subject to alternative independent inspection and, where available, the findings from such inspection.

Please feel free to contact me should you wish to discuss with us any of the comments we have made.

Yours sincerely



**Paul George**  
Director of Auditing and  
Director of the Professional Oversight Board  
DDI: 020 7492 2340  
Email: [p.george@frc-pob.org.uk](mailto:p.george@frc-pob.org.uk)

## Responses to specific matters raised in PCAOB Release No. 2008-007

### Part I

#### Rule amendments concerning the timing of certain inspections

*The Board is adopting an amendment to Rule 4003 that will give the Board the ability to postpone, for up to one year (i.e., to the end of 2009), first inspections of the remaining non-U.S. firms that the Board is currently required to conduct before the end of 2008. The Board is also proposing, and seeking comment on, an amendment that will give the Board the ability to postpone, for up to three years, first inspections that the Board is currently required to conduct before the end of 2009 in jurisdictions where the Board has conducted no inspections before 2009.*

We believe that the actions proposed by the PCAOB in relation to first time inspections are a pragmatic response to the specific challenges it has faced in conducting such inspections. However, we also believe that there is an urgent need for the PCAOB to broaden its proposals to include actions necessary to meet the challenges of further inspections of firms already inspected once, and actions aimed at moving towards a full reliance approach, as envisaged by its consultation on Rule 4012 and comments received thereon.

### Part II

#### Registered firms' obligations

*The Board recognizes that a refusal to provide information based on non-U.S. legal restrictions or the sovereignty concerns of local authorities implicates considerations not present in other non-cooperation circumstances. The Board invites public comment generally on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006.*

In our view, full account of all circumstances including information made available to the PCAOB on the conduct of inspections undertaken by the firm's national regulator should be taken in determining what, if any, sanction should be imposed on a firm for not co-operating with the PCAOB in an inspection.

*The Board is also considering whether there are possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information. One example that the Board has begun to consider would involve requiring a principal auditor to make certain public disclosures as part of, or in connection with, each audit report it issues for an issuer.*

*The Board invites comment on the potential benefits and drawbacks of a rule along the lines described above. The Board also invites comment more generally on other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest.*

We do not believe that disclosures of the type proposed would provide useful information to investors since they would not be in a position to make an informed assessment of any implications for the reliability of the audit opinions to which the disclosures relate. Disclosures relating to another firm whose work has been used by the group auditor would be particularly inappropriate, in our view, where the group auditor assumes full responsibility for the group audit. We are concerned that these proposals are inconsistent with the PCAOB's approach towards the inspection of auditors of significant subsidiaries who are not also auditors of US issuers. Further, such disclosures may have an adverse impact on investor confidence in the reliability of audit opinions where this is not merited and therefore would not be in the public interest.

We believe that the practical problems faced by the PCAOB in conducting inspections of non-US firms, to which the proposals are looking to respond, should reduce significantly if it moves quickly towards placing full reliance on the work of audit regulators in other jurisdictions, where appropriate. We therefore urge the Board to focus its attention on taking forward its proposed Policy Statement on moving towards a full reliance approach as soon as possible.