



Via Email

July 30, 2015

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

*Re: Supplemental Request for Comment: Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form (PCAOB Rulemaking Docket Matter No. 029)*¹

Dear Madam Secretary:

The Council of Institutional Investors (“CII”) appreciates the opportunity to provide comments on the Public Company Accounting Oversight Board’s (“PCAOB” or “Board”) supplemental request for comment on rules to require disclosure of certain audit participants on a new PCAOB form (“Proposed Rules”).² CII is a non-profit, non-partisan, association of pension funds, other employee benefit funds, endowments and foundations with combined assets that exceed \$3 trillion.³

As the leading voice for effective corporate governance and strong shareholder rights, CII believes that accurate and reliable audited financial statements are critical to investors in making informed investment decisions, and vital to the overall well-being of our capital markets.⁴ That strong belief is reflected in the following CII membership-approved policy on the “Independence of Accounting and Auditing Standard Setters”:

Audited financial statements including related disclosures are a critical source of information to institutional investors making investment decisions. The efficiency of global markets—and the well-being of the investors who entrust their financial present and future to those markets—depends, in significant part, on the quality, comparability and reliability of the information provided by audited financial statements and disclosures. The quality, comparability and reliability of that information, in turn, depends directly on the quality of the . . . standards that . . . auditors use in providing assurance that the preparers’ recognition, measurement and disclosures are free of material misstatements or omissions.⁵

¹ PCAOB Release No. 2015-004 (June 30, 2015), http://pcaobus.org/Rules/Rulemaking/Docket029/Release_2015_004.pdf.

² *Id.* at 1.

³ For more information about the Council of Institutional Investors (“CII”), please visit CII’s website at <http://www.cii.org/>.

⁴ Council of Institutional Investors, Policies on Other Issues, Independence of Accounting and Auditing Standard Setters (Adopted Oct. 7, 2008), http://www.cii.org/policies_other_issues#indep_acct_audit_standards.

⁵ *Id.*

This policy establishes the principle that “investors are the key customer of audited financial reports and, therefore, the primary role of audited financial reports should be to satisfy in a timely manner investors’ information needs.”⁶ Our membership reaffirmed that principle in 2013 when it approved substantial revisions to our policy on “auditor independence”.⁷ That policy includes the following provisions that we believe are relevant to issues raised by the Proposed Rules:

2.13a Audit Committee Responsibilities Regarding Independent

Auditors: The audit committee should fully exercise its authority to hire, compensate, oversee and, if necessary, terminate the company’s independent auditor. In doing so, the committee should take proactive steps to promote auditor independence and audit quality. Even in the absence of egregious reasons, the committee should consider the appropriateness of periodically changing the auditor, bearing in mind factors that include, but are not limited to:

....

- the track record of the lead partners and the extent of their professional commitments, as provided upon request or observable through disclosure or signature of the lead partner on the auditor’s report

....

Investors are the “customers” and end users of financial statements and disclosures in the public capital markets. Both the audit committee and the auditor should recognize this principle.

....

2.13f Shareowner Votes on the Board’s Choice of Outside Auditor:

Audit committee charters should provide for annual shareowner votes on the board’s choice of independent, external auditor. Such provisions should state that if the board’s selection fails to achieve the support of a majority of the for-and-against votes cast, the audit committee should: (1) take the shareowners’ views into consideration and reconsider its choice of auditor and (2) solicit the views of major shareowners to determine why broad levels of shareowner support were not achieved.⁸

⁶ *Id.*

⁷ Council of Institutional Investors, Corporate Governance Policies § 2.13 Auditor Independence (last updated Apr. 1, 2015), http://www.cii.org/corp_gov_policies#BOD.

⁸ *Id.*

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Generally consistent with our policies, CII continues to strongly support requiring disclosure in the auditor's report of the signature or name of the engagement partner participating in the audit.⁹ As we have previously explained:

Our support is based on the Council's membership-approved policies. Those policies indicate that information about engagement partners' track record compiled as the result of requiring disclosure of the partner's name in the auditor's report would be relevant to our members as long-term shareowners in overseeing audit committees and determining how to cast votes on the more than two thousand proposals that are presented annually to shareowners on whether to ratify the board's choice of outside auditor.¹⁰

We, however, would not oppose as an alternative the Proposed Rules' mandated disclosure of the name of the engagement partner in new PCAOB Form AP. While mandated disclosure in Form AP is less likely to capture all of the potential benefits of disclosure of the signature or name in the auditor's report the proposed disclosure would potentially provide for the compilation, access, and review of information about the engagement partner's track record that would be useful to our members as long-term shareowners.¹¹

⁹ See Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Phoebe W. Brown, Office of the Secretary, Public Company Accounting Oversight Board 2 (Aug. 15, 2014) ("As we have indicated in several prior letters to the Board on this topic, the Council strongly supports *requiring* disclosure in the auditor's report of the name of the engagement partner.") [hereinafter Aug. 2014 Letter], http://pcaobus.org/Rules/Rulemaking/Docket029/069c_CII.pdf; see also Ann Yerger, Executive Director, Council of Institutional Investors, Statement at the PCAOB's Investor Advisory Group Meeting 148 (Oct. 20, 2014) ("nothing sharpens the mind like a signature or a name on a document . . . requiring this transparency would result in greater accountability. . . . greater due diligence . . . improved audit quality . . . [a]nd in turn, I believe this would strengthen confidence in financial statements"), http://pcaobus.org/News/Events/Documents/10202014_IAG/2014_IAG_Transcript.PDF.

¹⁰ Aug. 2014 Letter, *supra* note 9, at 3 (footnotes omitted).

¹¹ We note that requiring disclosure of the engagement partner's name or signature in the company's annual proxy statement is also less likely to capture all of the potential benefits of disclosure of the signature or name in the auditor's report and is also generally inconsistent with the language of CII's membership approved policy. See § 2.13a Audit Committee Responsibilities Regarding Independent Auditors; see *generally*, Possible Revisions to Audit Committee Disclosures, Securities Act Release No. 9862, Exchange Act Release No. 75,344, 80 Fed. Reg. 38,995, 39,001-07 (concept release July 8, 2015) (discusses and asks whether audit committees should disclose name the engagement partner), *available at* <http://www.gpo.gov/fdsys/pkg/FR-2015-07-08/pdf/2015-16639.pdf>; Francine McKenna, Regulators Issue Competing Proposals for Audit Partner Disclosure, MarketWatch 1 (July 7, 2015) (describing how the Securities and Exchange Commission and the Public Company Accounting Oversight Board are "at odds over the best way for public companies to disclose the name of their lead audit partner"), <http://www.marketwatch.com/story/regulators-issue-competing-proposals-for-audit-partner-disclosure-2015-07-07>.

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Our more detailed views in response to select questions contained in the “Opportunity for Public Comment” section of the Proposed Rules follows:¹²

- 1. Would disclosure on Form AP as described in this release achieve the same potential benefits of transparency and an increased sense of accountability as mandatory disclosure in the auditor's report? How do they compare? Would providing the disclosures on Form AP change how investors or other users would use the information?**¹³

While CII does not oppose disclosure on Form AP, it generally agrees with the Board that the Proposed Rules may not achieve the same potential benefits of transparency and an increased sense of accountability as would be achieved by mandatory disclosure in the auditor's report.¹⁴ More specifically, CII agrees that disclosure in the auditor's report would be more transparent because (1) the “required information would be disclosed in the primary vehicle by which the auditor communicates with investors and where other information about the audit is already found . . . and [(2) the information] would be available immediately upon filing with the SEC of a document containing the auditor's report.”¹⁵

In addition, CII agrees that disclosure in the auditor's report, as compared to disclosure in Form AP, would increase an engagement partner's sense of accountability because the “engagement partner would be involved in the preparation of the auditor's report, but may not be involved in the preparation of the form.”¹⁶ Finally, as CII has previously indicated, it is important to emphasize that the:

Council's position in favor of requiring disclosure in the auditor's report of the name of the engagement partner is generally supported by, among other sources, the recommendations and conclusions of the U.S. Department of Treasury's Advisory Committee on the Auditing Profession, the growing body of empirical research indicating that the requirement would enhance investor protection and provide useful information to investors, and the more than eight years of experience with a similar requirement in the European Union.¹⁷

¹² PCAOB Release No. 2015-004 at 16-18.

¹³ *Id.* at 16.

¹⁴ *Id.* at A2-25, A2-26 (describing “benefits to market participants related to timing and visibility of the disclosures” from a required disclosure of the name of the engagement partner in the auditor's report).

¹⁵ *Id.* at A2-25.; *see, e.g.*, Francine McKenna at 2 (“The PCAOB hosted database would be new and its site is not currently a regular stop for investors and others researching hundreds of thousands of companies in a short time period.”)

¹⁶ PCAOB Release No. 2015-004 at A2-25.

¹⁷ Aug. 2014 Letter, *supra* note 9, at 2 (footnotes omitted); *see* PCAOB Release No. 2015-004 at A2-9, A2-10, & A2-11 (providing additional empirical evidence generally indicating that disclosure of name of engagement partner could be beneficial to investors).

5. What search criteria and functionality would users want for information filed on Form AP? What additional criteria and functionality beyond what is described in Section IV of this release would be useful? Would third-party vendors provide additional functionality if the Board does not? Are there cost-effective ways to make the disclosure more broadly accessible to investors who may not be familiar with PCAOB forms?¹⁸

CII generally agrees with the Board that “[r]equiring disclosure in a separate PCAOB form may decrease the chances that investors and financial statement users would seek out the information.”¹⁹ CII also agrees that disclosing the name of the engagement partner in the auditor’s report, as opposed to Form AP, provides “certain benefits to market participants related to timing and visibility of the disclosures.”²⁰

CII also agrees with the Board that the proposed “Form AP approach may . . . require more effort for investors to find the information, and it thereby could impose higher search costs in some instances, given that the auditor’s report is the existing vehicle by which the auditor communicates with investors and is the place where other information about the audit is already found.”²¹ Thus, the search criteria and functionality of the information filed on Form AP is an important issue for investors and other potential users of the information.

CII believes the search criteria and functionality that investors and other users would likely want for the proposed information filed on Form AP include ease of access and the ability to download the search results. More specifically, to ensure ease of access we believe that no more than three steps should be required for investors and other users to navigate from the PCAOB home page to the search results. On this point, we agree with Matt Waldron of the CFA Institute, who has illustrated how a seven step process to obtain disclosure about the engagement partner from the PCAOB’s Website, as some had previously proposed, is neither transparent nor accessible.²²

CII also believes that the functionality of the Form AP approach should allow investors and other users to download the search information results. The ability to download the information would likely facilitate the use of the information by third party vendors.²³

¹⁸ PCAOB Release No. 2015-004 at 16-17.

¹⁹ *Id.* at A2-27.

²⁰ *Id.* at A2-25.

²¹ *Id.* at 17.

²² Matt Waldron, Navigating a Maze: Audit Profession’s Solution for Disclosing Engagement Partner, Market Integrity Insights, Views on the Integrity of Global Capital Markets, CFA Institute 3 (Mar. 11, 2014), <http://blogs.cfainstitute.org/marketintegrity/2014/03/11/navigating-a-maze-audit-professions-solution-for-disclosing-engagement-partner/>.

²³ See, e.g., Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Phoebe W. Brown, Office of Secretary, Public Company Accounting Oversight Board 3 (Mar. 17, 2014) (“We believe such disclosure would result in databases or compilations of information about the engagement partner that would be useful to investors.”), http://www.cii.org/files/issues_and_advocacy/correspondence/2014/03_17_14_CII_letter_to_PCAOB_improving_audits.pdf.

As indicated by the Board, those vendors could then link the engagement partner data to “other data points”²⁴ which, among other benefits, would “provide investors with a more precise signal about the quality of the audit and, therefore, the reliability of the financial statements.”²⁵

- 6. Is 30 calendar days after the filing of the auditor's report (and 10 calendar days in the case of an IPO) an appropriate amount of time for firms to file Forms AP? Should the deadline be shorter or longer? Why? Are there circumstances that might necessitate a different filing deadline? For example, should there be a longer deadline (e.g., 60 days) in the first year of implementation? Should the 10-day deadline apply whenever the auditor's report is included in a Securities Act registration statement, not just in the case of an IPO?**²⁶

CII generally believes that the proposed 30 calendar days after filing of the auditor’s report is too long for firms to file Forms AP. As indicated, we agree with the Board that one of the benefits of our preferred approach of disclosing the name of the engagement partner in the auditor’s report is that it provides the information on a more timely basis.²⁷ More timely information makes it more likely that investors will be able to consider the information in connection with their oversight and voting responsibilities as shareowners.²⁸

CII notes that the Board has proposed that firms file Forms AP within a shorter 10-day deadline for initial public offerings.²⁹ The Board does not appear to provide any basis as to why the shorter 10-day deadline would be impractical for the audits of other companies.³⁰ Moreover, the Board noted that some commentators suggested a far shorter period than the proposed 30 calendar days, “such as 4 days” following the completion of the audit.³¹ CII, therefore, would generally support a deadline of no more than 10 days after the date the auditor’s report is first included in a document filed with the Securities and Exchange Commission.

- 8. Does Form AP pose any specific issues for EGCs? Would disclosure of the required information on Form AP promote efficiency, competition, and capital formation if applied to EGCs? If so, how? How does disclosure on Form AP compare to disclosure in the auditor's report proposed in the 2013 Release in that regard? Would creating an exemption for audits of EGCs benefit or harm EGCs or their investors? Why?**³²

²⁴ PCAOB Release No. 2015-004 at A2-4.

²⁵ *Id.* at A2-6.

²⁶ *Id.* at 7.

²⁷ *Id.* at A2-25 (“The required information would be disclosed in the primary vehicle by which the auditor communicates with investors and whether other information about the audit is already found, and would be available immediately upon the filing with the SEC of a document containing the auditor’s report.”)

²⁸ Aug. 2014 Letter, *supra* note 9, at 3 (Noting that in the “midst of the 2013 proxy season” there was a lack of timely and complete information about an engagement partner who was “separated from KPMG for his involvement in providing non-public client information to a third party in exchange for cash.”).

²⁹ PCAOB Release No. 2015-004 at 8.

³⁰ *Id.* at 8-9.

³¹ *Id.* at 8.

³² *Id.* at 17.

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CII generally believes that the Proposed Rules, if adopted, should be applicable to the audits of all public companies, including emerging growth companies (“EGC”). We are currently unaware of any legitimate basis for excluding the audits of EGC from the Proposed Rules.³³

We agree with the Board that the Proposed Rules’ disclosure should benefit companies and their investors in the form of “a lower cost of capital relative to those companies whose auditor’s performance record suggests a higher risk.”³⁴ As indicated by PCAOB Chairman Doty, the Board’s conclusion is supported by, among other sources, the experience in many foreign jurisdictions where the identity of the engagement partner has long been provided to investors.³⁵

CII appreciates your consideration of our views in response to the Proposed Rules. Please do not hesitate to contact me if you have any questions or would like any additional information about the content of this letter.

Sincerely,

A handwritten signature in cursive script that reads "Jeff Mahoney".

Jeff Mahoney
General Counsel

³³ See, e.g., Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Phoebe W. Brown, Office of Secretary, Public Company Accounting Oversight Board 3 (Dec. 16, 2013) (“Opposing an exemption for audits of emerging growth companies in connection with PCAOB Rulemaking Docket Matter No. 034”), http://pcaobus.org/Rules/Rulemaking/Docket034/222b_CII.pdf.

³⁴ PCAOB Release No. 2015-004 at A2-6.

³⁵ James R. Doty, Chairman, PCAOB, Statement on the Supplemental Request for Comment: Rules to Require Disclosure of Certain Audit Participants on New PCAOB Form 1-2 (June 30, 2015) (“studies . . . show that disclosure of the name of the audit engagement partner has made a difference in foreign markets”), http://pcaobus.org/News/Speech/Pages/06302015_Doty_Transparency.aspx.