



EUROPEAN COMMISSION

Internal Market

Director General

Brussels,
Internal Market DG/GL D(2004) 1091

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington DC 20006-2803
United States of America

Dear Sirs,

**Subject : PCAOB Release No. 2003-024; PCAOB Rulemaking Docket Matter No. 13
Proposed rules relating to the oversight of non-U.S. public accounting
firms**

We are grateful for the opportunity to comment on the proposed rules relating to the oversight of non-U.S. public accounting firms. These rules proposed by the PCAOB have important effects on US-listed EU companies and EU audit firms. We make the following comments in the context of the importance that the European Commission attaches to a constructive and open regulatory dialogue between the United States and the European Union. Such a positive dialogue is crucial to ensure consistent worldwide regulation of public accounting firms based to the largest extent possible on home country oversight and control. Cooperation between international regulators is essential – but it must be based on mutual respect of each partner’s laws and jurisdiction.

We have closely examined the Release and in particular Rules 4011 and 5113. It contains several positive elements for building an EU-US co-operative approach relating the oversight of non-U.S. public accounting firms.

However, we believe that a number of issues in the Release can be improved so that the rules better reflect a “true partnership” in the regulation of public accounting firms in cross-border cases. This will ensure the necessary predictability to European audit regulators and oversight systems on the conditions and practical application of the cooperative approach. In particular, we are concerned about the following issues:

Inspections

- i. Rule 4011 “inspections of foreign registered accounting firms” clarifies the principles for the PCAOB’s assessment of foreign systems but the section-by-section analysis also emphasises that its principles and criteria are illustrative and not exhaustive. This could mean that other criteria could be used in addition giving the PCAOB rather an open-ended discretion to assess foreign systems. The result would be considerable uncertainty for the PCAOB’s foreign counterparts whose systems will be judged. This uncertainty is amplified by the notion of the sliding scale of involvement of the PCAOB in the oversight of foreign audit firms. The clear impression is that the only benchmark is the PCAOB’s own

structure and competences whereas it is clear that there are different ways to achieve the equivalent ends.

- ii. Under a true EU-US cooperative approach on auditor oversight based on effective equivalence of regulation and oversight, we do not consider the direct participation of PCAOB inspection personnel in EU quality assurance reviews to be necessary in every case. Although we believe that systematic participation might be of interest as a measure of mutual confidence building at the beginning, we doubt whether this needs to be done on a permanent basis. We also question whether both sides need to allocate resources to such foreign participation, in particular, once initial experiences have been positive. We understand that the PCAOB is mandated to carry out inspections, especially the application of US-GAAP and PCAOB auditing standards. However, direct participation by PCAOB inspectors is problematic for a number of legal reasons and could even cause constitutional difficulties in some Member States. Therefore, such participation must be in accordance and agreement of the authority of the Member State where the audit firm is located. As in the PCAOB's briefing paper, we would also like more emphasis in the Rule placed on the importance of the PCAOB and foreign oversight bodies drawing up joint work plans as the basis for joint cooperation. Furthermore, for those of the oversight systems considered to be in the top scale, participation of PCAOB personnel should be limited to cases where knowledge of US standards cannot be secured by any other means. In this context it would be helpful if the PCAOB clarified in its rules whether the designated expert could also be a home country expert in US accounting and auditing standards. In any case, once the SEC will recognise IAS/IFRS for US listing purposes the need for such expertise would seem unnecessary for EU issuers in the US.
- iii. Rule 4011b requires each foreign audit firm to submit a written petition describing the non-US system of oversight to assist the PCAOB in assessing this non-US system. We doubt whether such a procedure is efficient and would be in line with a true cooperative approach with foreign oversight bodies. To minimise bureaucracy we suggest the PCAOB obtains such information once directly from the foreign oversight bodies.

Investigations

Rule 5113 "reliance on investigations of non-U.S. authorities" indicates the PCAOB's willingness to cooperate with foreign investigative authorities. We also welcome that the PCAOB is prepared to rely on sanctions of foreign jurisdictions imposed on these audit firms. However, here again the conditions for such co-operation are not specified clearly enough and so there will be an unacceptable high degree of uncertainty on how cooperation on investigations will work. We also believe that foreign interference in judicial proceedings in another country is not appropriate and we suggest that this (mutual) principle should be introduced into rule 5113.

PCAOB assistance to EU oversight bodies

We would welcome a clear and unequivocal statement in the rules of its willingness to assist non-U.S. oversight bodies in the oversight of US audit firms in the same way as it demands foreign counterparts be willing to provide assistance to the PCAOB for audit firms established in their territory. The Release reduces the notion of reciprocal co-operation to a small section worded in an ambiguous way. In this regard, we would

welcome the inclusion of cooperative procedures with foreign oversight systems in the PCAOB rules, based on the principle of reciprocity.

Legal conflicts

The present drafting of the rules does not take account of the fact that there are potential conflicts of law between the concept of US oversight on foreign audit firms laid down in the proposed rules and domestic Member State laws. Unlike the PCAOB briefing paper (PCAOB Release No. 2003-020, 28 October 2003), the proposed rules on inspection and investigation of foreign accounting firms do not recognise that conflicts of law may occur (e.g. secrecy rules; confidentiality; employment laws ...). For example, in the PCAOB briefing paper there was a recognition that the PCAOB would work with the home country system "... to attempt to resolve potential conflicts of laws ... including the use of special procedures such as voluntary consents or waivers ...". There is no such language in the rules. This is an issue which is of crucial importance for the EU and therefore we urge their inclusion.

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To summarise, we would urge revision of the Release to take account of the points mentioned above with a view to making much clearer the reciprocal benefits of a real co-operative approach with the PCAOB. Our comments have in particular underlined that on the basis of the current draft our Member States and the audit firms established in their territory are uncertain as to what the co-operative approach would mean in practice.

We trust that our comments will help the definition of the PCAOB rules that form the basis for a full EU-US co-operative approach regarding auditor oversight. We are open to discuss these matters with you further in the near future.

Yours sincerely,

Alexander SCHAUB
Director-General