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September 7, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street NW
Washington, D.C. 20006

Re: Rulemaking Docket Matter No. 17

Mr. J. Gordon Seymour:

Ernst & Young LLP (EY) is pleased to comment on the *Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence, the Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles* and the *Implementation Schedule for Rule 3523* as requested in PCAOB Release No. 2007-008 dated July 24, 2007 (Release).

The Release proposes an amendment to Rule 3523, as originally adopted by the PCAOB in July of 2005, as well as an explanatory Note concerning the implementation of the Rule when a company undertakes its initial registration (IPO) of its securities with the Securities and Exchange Commission (SEC). The Release announces a further adjustment of the implementation schedule for Rule 3523 to allow for comment on these proposals.

The Release also proposes a new independence rule, Rule 3526, *Communication with Audit Committees Concerning Independence*. This proposal expands on the current requirements of Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees ("ISB No. 1"), and two related interpretations, ISB Interpretation 00-1 and ISB Interpretation 00-2, which were adopted by the PCAOB as interim independence standards.

The Release requests comments on all aspects of the proposals and, in particular, comments with regard to six specific questions.

We support the PCAOB's efforts to continue to provide and enhance guidance on the PCAOB Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (the Rules) and matters surrounding implementation, particularly, those aspects of the Rules that may impact, unnecessarily, a registrant's choices when seeking to make a change in the registered firm conducting its audit. We have previously submitted comments and provided views to the Staffs of both the PCAOB and SEC on the Rules and EY's understanding and implementation processes surrounding these Rules.

Additionally, we support the PCAOB's efforts to continue to encourage communication between auditors and audit committees concerning matters that might reasonably bear on the auditor's independence. We believe the proposal regarding communication to the audit committee associated with an accounting firm's initial engagement pursuant to the standards of the PCAOB will provide the audit committee with important, timely and relevant information in order for the audit committee to make an informed decision in selecting an accounting firm as the issuer's auditor.

Our comment letter herein responds to the requests and includes additional information as we considered necessary to explain our views.

1. Comments Regarding Proposed Amendments to Rule 3523

EY previously responded to and commented on the PCAOB *Concept Release Concerning Rule 3523* (Concept Release*)* which was issued by the PCAOB on April 3, 2007. In our comment letter on the Concept Release, dated May 18, 2007 (a copy of which is attached to this letter for your convenience), we indicated our support for a potential amendment to Rule 3523 to eliminate the words "audit and" from the first sentence of the Rule. Accordingly, we support the PCAOB proposal which incorporates this change. We believe that this change is a positive one for the reasons set forth in our comment letter of May 18, 2007; namely it potentially provides companies more flexibility and choice when desiring to change auditors. We agree with the comments made during the Board's open meeting on July 24, 2007 that this proposed change can remove an obstacle to selecting the best firm to meet a company's needs without any compromise to the basic issues surrounding independence. Based on the analysis outlined in our prior letter, we believe that providing a tax service to an individual during the audit period but prior to the start of the professional engagement period poses less of a threat to independence than other services to the corporate entity might pose during the same period.

We did not comment on the matter of specific relief in the event of an IPO in our May 18, 2007 comment letter, but we note that other commenters did offer views on this important issue. We have commented on this specific aspect of Rule 3523 in previous comment letters and in meetings with the PCAOB Staff. We support the Board's decision to add a Note to Rule 3523 clarifying the application of that Rule with respect to periods prior to the engagement of the registered independent accounting firm to perform an audit in accordance with PCAOB standards. We believe that this proposed change creates more certainty with respect to what services rendered to a privately held audit client are permissible and do not impair independence if that company determines in the future to undertake a registration under the US securities laws. We believe that this Note is consistent with the goal of making the PCAOB rules no broader than necessary to accomplish their desired result while remaining cognizant of the general principle that requires companies and their auditors to avoid circumstances that could reasonably be thought to impair independence. The PCAOB's proposed change aids by removing a potential issue which could pose an unnecessary barrier to registration under the US securities laws.

Without this change, privately held companies that undertake an IPO would find that routine tax services rendered to individuals in Financial Reporting Oversight Roles (FROR) by the company's existing auditors created independence violations under PCAOB rules, even though the company had no involvement in such engagements and, indeed, such services complied with the applicable auditor independence standards at the time they were provided.

With respect to the amendment to Rule 3523 and the Note we suggest the PCAOB consider broadening the Note to include other transactions that have the same potential impact as an IPO, namely reverse mergers and similar transactions.

The Release indicates the Board is interested in commenter's views concerning transition periods. In the Board's open meeting, a concern was raised that the transition period could extend beyond the completion of the initial audit engagement. We have addressed these matters below in our response to the Board's specific question concerning Rule 3523.

2. Comments Regarding Proposed Rule 3526

The Release notes a gap in the existing requirements under ISB No. 1 and the SEC and PCAOB rules for communications between the issuer's audit committee and an accounting firm concerning independence matters prior to the firm becoming the issuer's auditor. ISB No. 1 requires communication to the issuer's audit committee regarding all relationships between the auditor and its related entities and the company and its related entities that, in the auditor's professional judgment, may reasonably be thought to bear on the auditor's independence prior to the company's initial filing and at least annually thereafter. These communications are made for initial registrants before the initial filing date and cover all periods included in a registration statement for the initial public offering of securities. ISB No. 1 does not specify a timetable for providing annual written and oral communication about independence matters; however, the SEC rules on communication with audit committees require that all other material communications with management be communicated to audit committees prior to the filing of the audit report with the SEC.

Although ISB No. 1 does not specifically address communication on independence matters during the period an audit committee is evaluating and making its decision to initially retain an accounting firm as the issuer's auditor, existing SEC and PCAOB pre-approval rules require that the audit committee pre-approve all current and proposed services prior to or simultaneously with engaging an accounting firm as the issuer's auditor. In our experience, communication currently takes place between EY and an issuer's audit committee prior to accepting an initial engagement pursuant to the standards of the PCAOB, whether that engagement is a new client acceptance or an initial public offering of an existing private audit client of EY. This communication may not be the same in content, timing or manner of documentation in each instance, but EY is cognizant of the need to identify and address potential independence issues at

the earliest feasible date and to comply with applicable professional standards in the circumstances.

We concur with the Board's observation that there may be a gap in the communication of relevant information about an accounting firm's independence when the audit committee is considering multiple firms in making its decision to retain a new accounting firm as the issuer's auditor. While an audit committee may request, or an accounting firm may offer, relevant information about the firm's independence for consideration in making the decision, there may be differences in the form and content of the communication from the involved accounting firms. We believe providing relevant information to the audit committee about the accounting firm's independence will aid the audit committee in its decision making process when considering a change in auditor. In the case of an existing issuer considering a change in auditors, this earlier communication may offer additional independence information to the audit committee, in a reasonable timeframe, which would assist in its determination about whether to retain the firm as the company's auditor. However, in the proposed rule there is no specified time period over which an accounting firm should consider the relationships that might reasonably be thought to bear on independence with respect to a prospective new audit client. We believe that a time period should be specified and that the period should appropriately include the current period and the expected "audit and professional engagement period" bearing in mind that, in certain circumstances, other prior relationships may need to be considered. An auditor must consider the reasonable investor standard and its independence "in appearance" in the given circumstances. Using the current period and the expected "audit and professional engagement period" would take into account the specific circumstances, for example, if a given audit committee believed that it wanted the auditor to consider past relationships in the event of the need for re-audits of prior years for various reasons.

However, we believe Rule 3526, as currently proposed, could cause an undue burden on private companies pursuing IPOs if such communication is required prior to the acceptance of the engagement to assist an existing private audit client with its initial registration. Generally, in our experience, for an existing private audit client, the assessment under the SEC and PCAOB independence rules occurs simultaneously with the performance of the engagement to assist the company in preparing for its IPO. The independence assessment, particularly for multinational companies, may require significant time to complete. If a requirement existed for the independence assessment to be completed before any work could be commenced by the existing auditor related to the IPO, this might put the company at a disadvantage by causing a delay in the timing of its filing. We believe this work can proceed simultaneously and that the current timing of the required communication under ISB No. 1 in the case of an IPO is sufficient to allow the audit committee to properly assess the auditor's independence prior to the company's initial filing.

Currently under ISB No. 1, certain information is required to be reported to the audit committee if in the "*auditor's professional judgment*" it may reasonably be thought to bear on

independence. In making that determination, the auditor is currently required to consider not only relationships that are specifically proscribed by the SEC and PCAOB rules, but also the general standard of auditor independence and four fundamental principles set forth in the Preliminary Note to Rule 2-01 of Regulation S-X. Although the Board's stated intention for omitting these words is to "clarify the requirement by reminding auditors of the need to focus on the perceptions of reasonable third parties when making independence determinations," we believe the removal of this language may serve to confuse, rather than clarify, the requirement. Since the Board believes that the auditor will still "need to apply professional judgment to determine what is reasonable under particular facts and circumstances," consideration should be given to retaining the "auditor's professional judgment" language and making reference to the SEC general standard and four principles of auditor independence in the adopting release or the proposed rule.

Subject to the recommendation to maintain the standard of "*auditor's professional judgment*", we support the proposal's requirement for the auditor to (i) annually provide details in writing to the audit committee, (ii) have discussions with the audit committee, and (iii) document the substance of the discussions with the audit committee.

3. Responses to Specific Questions

The Release seeks responses to six specific questions. We have addressed these below.

A. Question 1

Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?

We believe the communication requirements under the proposed rule will likely assist the audit committee in fulfilling its obligations with respect to auditor independence, particularly when contemplating a change in auditor. However, it is unclear how the proposed rule would enhance compliance with the auditor independence requirements by registered firms. EY has policies, processes, and procedures in place, which are annual, periodic or event driven (e.g., IPO, new client acceptance, business combinations, change in control) to help ensure auditor independence during the applicable audit and professional engagement period. As a result, we do not believe that the differences between the proposed rule and the existing requirements under ISB No. 1 and the SEC and PCAOB rules would enhance EY's ability to fulfill its obligations with respect to auditor independence.

Under the proposed Rule 3526, an auditor would be required to communicate "*prior to accepting an initial engagement pursuant to the standards of the PCAOB.*" Currently

this communication occurs, as required by ISB No. 1, prior to a company's initial filing and at least annually thereafter. While services must be pre-approved prior to engaging an accounting firm as the issuer's auditor, there is no existing requirement to specifically communicate information on certain other relationships to the issuer's audit committee at the time it is making a decision regarding a change in auditor. The proposed rule would not change the firm's obligation to ensure that it is independent during the audit and professional engagement period prior to accepting a new audit client. However, since auditor independence is a mutual responsibility, the proposed rule may assist the audit committee with fulfilling its obligations with respect to auditor independence when considering a change in auditor.

As noted above, the timing of the required communication for private companies contemplating an IPO should be reconsidered as the acceleration of the timing of the communication from that which is currently required under ISB No. 1 may interfere with a company's ability to complete its IPO within its desired timeframe.

B. Question 2

Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?

We believe that requiring communication of certain information, similar to that required annually under ISB No. 1, prior to becoming an existing issuer's auditor will aid the audit committee in its decision making process. The proposed rule should serve to improve the consistency of information being received by audit committees from all accounting firms under consideration for selection. Consistency in the communication received by the audit committees would offer a comparative look at the accounting firms and their respective independence matters, understanding that the same types of relationships were considered and principles were applied, and that appropriate professional judgment was employed. The additional information and consistency of such information would help facilitate the audit committee's assessment regarding a firm's independence and decision about whether to retain an accounting firm as the issuer's auditor. The proposed requirements would serve to augment the discussions between the audit committee and the accounting firm(s) involved in the proposal process.

C. Question 3

Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what communications should the auditor be required to make to the audit committee?

Open and transparent communication is an important part of the relationship between the auditor and the audit committee. It helps to ensure that both parties have the information necessary to fulfill their shared responsibility as it relates to independence. We believe the information concerning independence currently required to be communicated under ISB No. 1, enhanced by the change in the timing of the required communication for a change in auditor of an existing issuer under proposed Rule 3526, would be sufficient for the audit committee to fulfill its obligations with respect to auditor independence. We do not believe that additional information is necessary to accomplish the Board's objective and, in fact, could unnecessarily overburden the audit committee. The communication should disclose information that is useful and relevant to a particular company's audit committee and we would continue to encourage audit committees to request additional information to fulfill the specific needs of that audit committee or issuer.

D. Question 4

To what extent, if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?

Registered accounting firms are required by ISB No. 1 to communicate relevant information related to the firm's independence to the audit committees of its issuer audit clients. In our experience, discussions between the audit committee and EY generally occur in connection with IPOs, changes in auditors to EY, at least annually for EY issuer audit clients, and with respect to significant transactions in which an issuer audit client engages (for example with respect to an acquisition). We communicate to audit committees those financial, employment, and business relationships, and services and fee arrangements during the audit and professional engagement period that, in our professional judgment, may reasonably be thought to bear on independence, taking into consideration the particular facts and circumstances and available guidance from the SEC and PCAOB. In addition, accounting firms are required to communicate information on the scope of proposed services and fee arrangements sufficient for the audit committee to make its own determination regarding the permissibility of such service and fee arrangement, pursuant to SEC and PCAOB pre-approval rules including PCAOB Rules 3524 and 3525 which cover specific pre-approval requirements for certain non-audit services.

EY's communications with audit committees are not limited to the required formal communications but also generally consist of frequent informal dialogue and discussion with the audit committee about independence related matters. These informal communications, which may be initiated either by us or the audit committee, assist both parties in fulfilling their mutual responsibility for auditor independence.

Accounting firms may not, necessarily, be communicating the same information as required under ISB No. 1 to audit committees prior to being engaged as the auditor of an issuer unless requested by the issuer's audit committee. EY's current policy is to assess such relationships and evaluate whether we are independent under the applicable SEC and PCAOB rules for the anticipated audit and professional engagement period(s) and communicate our findings to the audit committee prior to accepting an issuer as a new audit client or prior to the filing of an initial registration statement under the SEC rules for an existing private audit client.

E. Question 5

Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why and how long should the period be?

Information regarding certain relationships is used by the audit committee to assess an auditor's independence during the expected audit and professional engagement period, as defined by the SEC. The initial communication under proposed Rule 3526(a) should require the disclosure and discussion of information for the timeframe that is of relevance to the audit committee. We believe that prior to filing an initial registration or making a decision to retain a new accounting firm, the relevant relationships are those that exist currently, or will continue to exist, during the expected audit and professional engagement period. Since the relationships that may potentially bear on an accounting firm's independence are generally limited to those that exist during the audit and professional engagement period, requiring identification and communication of relationships existing prior to this period would cause an unnecessary burden on the accounting firm to identify and communicate these matters, and on the audit committee to consider such information, bearing in mind that the accounting firm was not subject to the auditor independence rules with respect to this company at that prior time. We recognize that in certain instances an issuer may request that the accounting firm provide relevant information about a longer period; such would be the case if the audit committee needed to have information about the firm's ability to potentially audit restated financial statements for prior years for various reasons.

Once an independence matter is communicated to the audit committee in writing, we do not believe it is necessary to repeat the communication of this matter unless the matter continues to exist in a future audit period or is an on-going matter. We recognize that audit committee members may change from time to time; however, the continuing or prior audit committee members may inform the new members of the matters that they believe have a bearing on auditor independence on a going forward basis.

Although certain services rendered by an accounting firm prior to the start of the audit and professional engagement period may continue to have an effect on the issuer's financial statements, such services would not impair the successor auditor's independence and should not be required to be communicated under proposed Rule 3526. Examples of services that may have a continuing impact on future periods include appraisals, valuations, Section 404 related procedures, and financial information systems design and implementation. If the results of those services were subject to audit by the predecessor auditor, we believe that disclosure of such services would not be warranted since the services would have no bearing on the independence of the potential successor auditor. Comments made by Michael W. Husich, Associate Chief Accountant, Office of the Chief Accountant, in a speech on December 11, 2006 at the AICPA National Conference on Current SEC and PCAOB Developments and a recent FAQ issued by the Staff of the SEC on August 6, 2007 on prohibited and non-audit services, support the thinking that such services would not need to be disclosed in the initial communication since the successor auditor's independence would not be impaired.

F. Question 6

Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?

Current PCAOB Rule 3523(c) contains a transition rule which addresses the appropriate time period for a registered accounting firm to complete or otherwise terminate tax services provided to a person who becomes an FROR due to a "change in employment event". That transition period is 180 days, provided the work was being performed pursuant to a previously existing engagement on which work of substance has been performed. A previously existing engagement implies an engagement in progress as opposed to an existing client relationship where there is no current work being performed. We believe that a transition period is appropriate for purposes of Rule 3523 for engagements in process at the time of initial engagement to perform an audit in accordance with the standards of the PCAOB. This transition period should cover not only the new auditor situation and the IPO situation contemplated by the Note to Rule 3523, but also other events that may result in the initial application of the Rule, such as a subsidiary previously deemed immaterial becoming material or a new equity-based transaction occurring which causes the company being audited to become subject to the provisions of Rule 3523. The application of a transition period would be beneficial to both audit clients and FRORs who could find their compliance with all relevant tax requirements threatened by the current and proposed PCAOB Rules.

The Board has already identified 180 days as an appropriate transition period for services rendered pursuant to change in employment events. This time period could allow tax services to be provided to an FROR during the period when audit services are being provided to the issuer. Thus, the Board has already evaluated the independence risk concerning tax services provided to persons in an FROR role and concluded that reasonable transition periods are an important aspect of the Rule. If a company were to hire a new CFO, the existing auditor would be permitted under the current Rule to continue to provide service to that individual for 180 days. To provide a shorter or different period for new audit engagements or initial public offerings would serve to add an unnecessary complexity and inconsistency to the PCAOB Rules. Therefore, we support a consistent transition period for all situations where one is needed and we believe that the situations contemplated by the Board's proposed amendments to Rule 3523 are situations where a transition period is needed.

Companies are increasingly global in scope and the definition of FROR could include employees around the world. At the time a firm would be engaged as auditor, it would be possible for that firm to have several tax services engagements in process to FRORs in different countries of the world. Different tax regimes exist with many different filing dates. The accounting firm and the company should be aware of the relationships that exist as of the date of the appointment, but some of those engagements may not be able to be terminated without considerable cost or inconvenience to the FROR. While the start of the professional engagement period can be managed to a certain degree by the timing of the signing of the engagement letter or the initiation of audit procedures, this does not offer sufficient flexibility to address practical situations. Further, a delay in the start of the professional engagement period in order to terminate various personal tax services would possibly create a situation where the new accounting firm has less time to become familiar with the company's books and records prior to issuing its first report or completing a quarterly review. In the United States, a personal tax return is due 3 ½ months after the beginning of the year. Upon request, the tax return due date can be extended for an additional 6 months. Thus, the process of preparing a tax return for a client in the US can span 9 ½ months. In other parts of the world, the due dates for personal tax returns are not consistent with April 15, and, in many jurisdictions, extensions of the filing deadline are not permitted. Thus, the requirement of a "hard stop" on the date of the appointment as auditors could cause hardship and lead to situations where registered public accounting firms and audit committees are forced to deal with such matters which do not compromise the basic issues surrounding auditor independence.

Forcing tax service provider changes within a short time period can have an impact on the FROR who potentially could be facing two significant issues:

- The need to complete the existing tax engagement and ensure he or she complies with the relevant tax laws to timely file the associated returns.
- The need to find a new qualified tax service provider.

The combination of these two activities can be difficult for an FROR if sufficient time is not available especially since the time available to resolve these issues is not within the control of the FROR.

The same timing and global issues regarding the audit client discussed above may force the FROR to turn to another provider prior to the completion of a tax engagement. Switching to a new tax service provider prior to the completion of an existing tax engagement can create duplicate time, effort and costs to the FROR. Additional time should be allowed to complete work in progress to alleviate a significant portion of this duplication of time, effort and cost. The application of a transition period similar to the one currently provided within Rule 3523(c)(2) would allow sufficient time for the completion of work in progress without adding any additional risk than is currently had with a change in employment status.

In addition to the time, effort and cost to the FROR, there is the additional risk that the FROR may find it difficult to immediately find a qualified replacement for tax services provided by the current audit firm. Without a sufficient transition period, the FROR may be faced with the need to rush with the identification of competent replacements, review such choices, and then make a selection of the most appropriate replacement. Furthermore, in many global assignments, the choices available to the FROR may be limited due to independence or other reasons relevant to the issuer.

Undoubtedly, there is a need to transition to a new tax service provider in these situations. The question is whether the FROR should be faced with the difficult task of doing this within a very limited time period when he or she also has pressing needs to have an existing tax engagement completed. The added complexity of choosing an appropriate replacement provider warrants the need for a transition period. There needs to be sufficient time to ensure that a complete and accurate assessment can be completed before a decision as to the new tax service provider is made. The risk of additional time, effort, cost and the potential of choosing an inappropriate tax service provider due to time constraints out of the FROR's control outweighs any small risks involved by providing a transition period similar to what is provided within current Rule 3523(c)(2).

The Board's proposals encompassed in Rule 3526 would offer the accounting firm and the audit committee an opportunity to assess the permitted tax services rendered to FRORs and to determine if limitations on those services during the transition period are warranted. For instance, the audit committee might decide that the tax services could be

limited to tax return preparation only as opposed to tax planning. Alternatively, the audit committee might decide to require a shorter time period for transition.

We encourage the PCAOB to consider a broad application of a transition period to include other situations in which a company or an individual first becomes subject to Rule 3523. Merger and acquisition transactions during the year may cause similar challenges to those described above for individuals who are FRORs at companies involved in the transactions. Such transactions may be more problematic than a change in auditor situation, in which it may be possible to delay the start of the engagement period, because a transaction date may not be flexible due to financing or other business reasons. In addition, FRORs at a subsidiary that becomes material to the consolidated financial statements for the first time during the year may not be aware they are subject to the Rule until after year end. Without a transition period for these types of situations, the potential exists for many inadvertent violations of Rule 3523, even though such situations may have no more of an effect on auditor independence than services provided during a change in employment event.

We recognize in certain very rare instances tax services that have been provided to individuals in an FROR role in the audit period may have an impact on the financial statements of the audit client. Such rare circumstances could be where the tax services include advice on transactions where there may be a mutuality of interest or conflicting positions between the tax treatment of the individual and that of the employer. This could be the situation in an IPO environment where the auditor could be advising the FRORs about personal tax matters and where the tax effect to the FRORs and shareholders is impacted by decisions the company makes. We believe these circumstances, if they exist, would warrant more consideration and evaluation from an independence perspective but we believe that the assessment should be based on the existence of the service or the relationship, and made jointly by the independent accounting firm and the audit committee. This assessment could conclude as to an appropriate transition period for the services within the period allowed by the PCAOB.

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Conclusion

For the reasons cited above, Ernst & Young LLP strongly supports the proposal to amend Rule 3523 to strike the words “audit and” from the current text of Rule 3523. We also support the addition of the proposed Note concerning initial public offerings to Rule 3523 with the additional recommendation that the Board consider transactions and events which are equivalent to IPOs. We believe this is a reasoned approach and one that does not fundamentally impact independence.

We also urge the Board to consider a modification to add a transition period to the Rule. We support a Board clarification that treats an "initial engagement to perform an audit pursuant to the standards of the PCAOB, similar to that of a "change in employment event" as that term is defined in Rule 3523(c). This clarification would allow for the time limited exception to the rule to come to bear. We believe this change would improve standardization of the Rule provisions within Rule 3523(c) while maintaining the overall protection originally intended by the Rule. Given the rationale previously stated, we believe a standard transition period is more appropriate than multiple Rules to address different situations. The potential impact on independence is not different and a similar approach simplifies the application of the Rule in otherwise complex situations.

We also fully support the Board's efforts to encourage communication regarding independence matters between the accounting firm and the audit committee. We support the intent of proposed Rule 3526 to require appropriate information concerning the accounting firm's independence to be communicated to the issuer's audit committee at the time that the audit committee is making the decision to retain the accounting firm as the issuer's auditor. We request the Board reconsider the timing requirements of the proposed Rule which could apply in the event of an IPO, including clarifying the requirements so that a company's decision to register shares is not unduly delayed while an audit firm evaluates its independence under the rules of the PCAOB, and that the Board consider specifying the time period of the consideration in an initial appointment circumstance to be the current period and the expected audit and professional engagement period. This would take into account, depending on the specific circumstances and the audit committee's interests and expectations, that this could include multiple periods including some in the past in the event of the possible need for re-audits for a variety of reasons.

We would be pleased to provide the Board with additional information on these matters and our views as addressed by this letter.

Respectfully submitted,

Ernst & Young LLP

Attachment

Attachment

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May 18, 2007

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

Re: Rulemaking Docket Matter No. 17

Mr. J. Gordon Seymour:

Ernst & Young LLP (EY) is pleased to comment on the *Concept Release Concerning Scope of Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles, Implementation Schedule for Rule 3523* as requested in PCAOB Release No. 2007-002 dated April 3, 2007. We support the PCAOB's efforts to provide and enhance guidance on the PCAOB Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (the Rules) and matters surrounding implementation, particularly those aspects of the Rules that may unnecessarily impact registrant's choices when seeking to make a change in the registered firm conducting its audit. We have previously submitted comments and provided views to the Staffs of both the PCAOB and SEC on the Rules and our Firm's understanding and implementation processes surrounding these Rules.

The Concept Release indicates the Board is interested in views on whether the distinction that Rule 3523 relates to services provided to individuals and not to the audit client directly has a bearing on the nature and the extent of any independence concerns that may exist with respect to tax services provided during the audit period to persons covered by Rule 3523. The Concept Release seeks responses to two specific questions.

We have addressed these matters below:

1. Question 1

> **To what extent, if any, is a firm's independence affected when the firm, or an affiliate of the firm, has provided tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the professional engagement period?**

As the Board notes, under currently existing Rule 3523, if a registered firm provides tax services during the audit period, but before the commencement of the professional engagement period, this is an impairment of independence and this violation cannot be remedied by the registered firm's ceasing to provide the tax services before accepting the engagement. Accordingly, in this circumstance, the registered firm may not become the auditor to the company. This is consistent with the SEC's auditor independence rules regarding proscribed services—i.e. that an accountant is not independent if prohibited services are provided during the audit and professional engagement period. However, a recent speech by Mr. Michael Husich, Associate Chief Accountant, Office of the Chief Accountant, provides important new thinking on this point. Mr. Husich states that in instances of potential auditor change, this occurrence will not operate to deem an accountant not independent when certain services are provided in the audit period, but prior to being appointed the auditor, so long as such services:

- relate solely to the prior period which is audited by a predecessor auditor
- will not be subject to audit procedures by the successor auditor, and
- are not management functions.[1]

With respect to the tax services contemplated by Rule 3523, the criteria above can, in most instances, be easily applied leading to enhanced consistency with the recent views of the Staff as expressed in Mr. Husich's speech. If tax services have been provided to individuals in financial reporting oversight roles (FROR) during the audit period, but prior to being appointed the auditor, applying the above criteria addresses the potential of an independence threat based on the principles of independence as found in the Preliminary Note to Regulation S-X, Rule 2-01 (b) which states.

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[1] Speech by Mr. Michael Husich, December 11, 2006 at the AICPA National Conference on Current SEC and PCAOB Developments. "I have a few comments concerning three matters, for which additional guidance is being considered**.** First, five of the prohibited services delineated in Rule 2-01(c)(4) (bookkeeping, financial information system design and implementation, appraisal or valuation services, actuarial services, and internal audit outsourcing services) have an exception condition, "unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the client's financial statements", also known as the "not subject to audit" provision. **The staff's position is that a successor auditor's independence would not be impaired if the successor auditor provided prohibited non-audit services in the current audit period and these services (i) relate solely to the prior period which is audited by a predecessor auditor, (ii) will not be subject to audit procedures by the successor auditor, and (iii) are not management functions." (emphasis added)**

> "In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service: creates a mutual or conflicting interest between the accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client."

While the services contemplated by Rule 3523 do not necessarily have the safeguard of being subject to the audit procedures of the predecessor auditor, they are not services provided to the audit client but, rather, to individuals who serve in FROR roles at the audit client. Indeed, it would be rare that the results of tax services provided to an individual in an FROR role would impact the financial statements at all. The fact that these services are provided to the individual and not to the audit client act to counter any mutuality of interest.

We believe the Board's concept release has recognized the significant and compelling difference between services provided to an individual who is in an FROR role and services provided directly to the audit client. The Board has already, in part, differentiated these services, as Rule 3523 has a time limited exception in Rule 3523(c) which permits continuation of a tax services engagement to a person who becomes subject to Rule 3523 due to certain changes in the individual's employment (employment events). This time limited exception already recognizes that tax services provided to an individual in an FROR role can be continued during an audit period without immediately impairing independence. We concur that services rendered to an individual in an FROR role, prior to an auditor appointment, are fundamentally different from services provided directly to an audit client. It is our view that if the Board determined to amend Rule 3523 to only encompass the "professional engagement period" as opposed to the "audit and professional engagement period" such change will not raise any new or additional independence considerations surrounding personal tax services to individuals in an FROR role. We find this consistent with the direction of Mr. Husich's speech cited above and we find that direction an appropriate balance between the importance of an auditor's independence and the ability of registrants to have adequate choices in auditor selection and not be impeded in such choices by services that do not fundamentally affect auditor independence as they were commenced and, in many cases delivered, prior to being considered to be the auditor.

We recognize in certain rare instances tax services that have been provided to individuals in an FROR role in the audit period may have an impact on the financial statements of the audit client. Such rare circumstances could be where

the tax services include advice on transactions where there may be a mutuality of interest or conflicting positions between the tax treatment for the individual and that of the employer. Should such rare circumstances arise, they could create a situation where tax services to an individual in an FROR role create the potential for an independence concern. This situation was noted in comments of the Internal Revenue Service, the Securities and Exchange Commission and the PCAOB in February 2005 concerning the transactions entered into by certain taxpayers concerning executive stock options[2]. We believe these circumstances are rare following both the reforms of the Sarbanes-Oxley Act, the PCAOB's rulemaking and operational changes incorporated into the tax practices of many accounting firms. We believe these circumstances, if they exist, would warrant more consideration and evaluation from an independence perspective prior to client acceptance but believe that the assessment should be based on the existence of the service or the relationship, not the time frame in which the service was rendered and are adequately provided for in existing literature and guidance.

2. Question 2

What effect, if any, would application of Rule 3523 to the audit period have on a company's ability to make scheduled or unscheduled changes in auditors? Could any such effect be minimized or managed through advanced planning or otherwise?

This question in the Concept Release focuses on a company's ability to make scheduled or unscheduled changes in its auditors based on the application of Rule 3523 to the audit period. An auditor change may occur relatively quickly and often under a high degree of confidentiality. This can occur in transaction driven situations and other circumstances. In other instances, the decision to consider an auditor change is made well in advance. Where possible, advance planning would minimize an effect of Rule 3523. However, advance planning is not always possible. Further, for confidentiality reasons, not all individuals in an FROR role may be informed of a company's possible evaluation of changes in its auditor.

We believe application of Rule 3523 to the audit period would serve to limit a company's potential choices among auditors. We believe this is not in the best interests of shareholders and other participants in the capital markets. Approximately 70% of the Fortune 1000 companies report their financial results on a calendar year basis. For such companies, the audit period begins January 1

[2] IR 2005-17 February 22, 2005 Settlement Offer Extended for Executive Stock Option Scheme and comments of the PCAOB and SEC.

and continues to December 31. Any plan to consider a change in auditor initiated after January 1 exposes the company to have fewer potential firms that can perform the audit due to the application of Rule 3523 to the audit period. In addition, considering the tax filing deadline in the United States, the selection process may coincide with and overlap with April 15th - the initial deadline for U.S. personal income tax returns. It is likely that an auditor selection process which started March 1 would find that several firms would not be independent due to tax services provided to individuals in an FROR role for a period after January 1 of that year.

The above example only addresses the potential impact of the audit period beginning prior to the professional engagement period for U.S. tax compliance services in calendar year audit situations. Further conflicts will also be created when dealing with various foreign tax compliance filing requirement dates for individuals in FROR roles and/or audit clients with other than calendar year ends. As an example, in many foreign jurisdictions, there is no mechanism for the extension of tax return filing deadlines. Therefore, an announced auditor change could potentially place an individual in an FROR role in a position of considerable hardship to file a tax return on a timely basis. Absent an appropriate transition rule, the individual in an FROR role may be forced, under extreme time constraints and at a significant cost, to identify a new service provider.

We believe the hardship imposed on companies by the current provisions of Rule 3523 exist whether the auditor change is scheduled or unscheduled. Unscheduled changes often occur in a tight timeframe and provide many other issues beyond tax services to individuals in FROR roles. In the case of scheduled changes, the additional time may simplify the issue, but, often, does not. There may be more than one potential audit firm (especially in global organizations) providing tax services to individuals in FROR roles at the time of commencement of an evaluation of auditors. Even with advance planning, it is possible that confidentiality concerns may create difficulties in determining whether a potential audit firm is providing services to individuals in an FROR role. The definition of who is an FROR covers a range of individuals at both the parent company and its material subsidiaries and affiliates around the world. Should an auditor have to communicate to an individual tax service client that independence concerns relating to a possible auditor change make it impossible for the audit firm to provide the individual with tax service, that auditing firm could find itself in a position of violating a request for confidentiality during the proposal process. Again, this would be an example of putting a potential audit firm and the company in an impractical position.

Given that companies often use multiple non-audit service providers, continued application of the provisions of Rule 3523 could lead to circumstances where not only is the company restricted in its choice of audit providers but individuals in FROR roles are restricted in their choice of tax service providers. Without this revision, it is possible that companies would adopt a policy of restricting individuals in FROR roles from using the tax services of certain audit firms. This creates a lack of choice for these individuals and quite possibly denies them access to the specialized tax services they may require.

Conclusion

For the reasons cited above Ernst & Young would strongly support if the Board determined to amend Rule 3523 to strike the words "audit and" from the current text of Rule 3523 (as identified in footnote 9 of the Concept Release). We believe this is a reasoned approach and one that does not fundamentally impact independence.

We also urge the Board to consider a further but related modification. We support a Board clarification that treats a change in auditor in a manner similar to that of a "change in employment event" as that term is defined in Rule 3523 (c). This clarification would allow the time limited exception to the rule to come to bear. We believe this change would improve standardization of the Rule provisions within Rule 3523 (c) while maintaining the overall protection originally intended by the Rule. Given the rationale previously stated, we believe a standard transition period is more appropriate than multiple rules to address different situations. The potential impact on independence is not different and a similar approach simplifies the application of the Rule in otherwise complex situations.

We would be pleased to provide the Board with additional information on the matters and our views as addressed by this letter.

Respectfully submitted,

Ernst & Young LLP