Matthew J. Foehr
Vice President and
Comptroller

Chevron Corporation
6001 Bollinger Canyon Road
San Ramon, CA 94583
Tel 925 842 3232
Fax 925 842 2280

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Via email to comments@pcaobus.org

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 37

Chevron Corporation ("Chevron") appreciates the opportunity to provide comments to the PCAOB on the concept release on possible revisions to PCAOB ("Board") standards related to mandatory audit firm rotation – Rulemaking Docket Matter No. 37.

Chevron is a global, integrated energy company based in San Ramon, California. The company explores for, produces and transports crude oil and natural gas; refines, markets and distributes transportation fuels and other energy products; manufactures and sells petrochemical products; generates power and produces geothermal energy; provides energy efficiency solutions; and develops the energy resources of the future, including biofuels. The company's activities are widely dispersed geographically with operations in North America, South America, Africa, Asia, Australia and Europe.

We appreciate the PCAOB's continued efforts to ensure investor access to accurate information on publicly listed companies and their financial performance. We agree that auditor independence, objectivity and professional skepticism are important in supporting the communication of companies' operations and results to the public. However, we strongly believe that the PCAOB's proposal for mandatory audit firm rotation is impractical and insufficiently justified from a cost-benefit perspective. In addition, we believe it will not result in enhancements to audit quality beyond those already achieved through the implementation of relevant Sarbanes-Oxley ("SOX") provisions and, in fact, will increase the risk of audit deficiencies or failures to the detriment of investors and the public.

As chronicled in the PCAOB concept release, mandatory audit rotation has been debated for decades. During this extended period of debate there has been no convincing evidence that the purported benefits of mandatory audit rotation outweigh the considerable incremental costs and risks. We do not believe that arguments supporting the concept of audit firm rotation have significantly changed since Congress' rejection of this concept during deliberation of the Sarbanes-Oxley Act in 2002, or since publication of the General Accounting Office study in November 2003.

According to the concept release, the PCAOB's rationale for considering mandatory audit rotations is to ensure an appropriate independent relationship between the audit firm and the audit client. This assurance has already been accomplished through SOX Sections 203 and 301. SOX Section 203 required audit partner rotation on a five year basis with a five year "time-out." The SEC noted in its adoption of the

rules supporting SOX Section 203 that such mandatory partner rotation was an appropriate mechanism for providing a fresh look at the independence of the audit engagement while balancing the continuity of an audit firm's institutional knowledge and expertise.[1] SOX Section 203 and the accompanying SEC rules were instituted in order to address the exact same issues for which mandatory audit firm rotations are now under reconsideration to address.

SOX Section 301 specifies that the Audit Committee has the responsibility for appointment, compensation, and oversight of the company's audit firm. The Audit Committee is therefore responsible for evaluating the effectiveness of the audit engagement team. The charter of the Chevron Audit Committee explicitly states that a key purpose of the committee is to "assure that the Corporation's financial statements are properly and cost effectively audited by qualified accountants who are independent." The Committee is also responsible for annually selecting and employing the Corporation's independent auditor. In this capacity, we believe that the Audit Committee is best qualified to determine when it may be appropriate for the company to change audit firms.

The disadvantages to audit firm rotation are numerous, which is why the decision needs to be weighed carefully by individuals, such as members of the Audit Committee, who are knowledgeable about a company's particular circumstances.

Chevron conducts business in a complex industry with extensive global operations. Many locations and joint ventures have complex fiscal and tax requirements. A familiarity and understanding of both the energy industry and the company are necessary for effective auditing, and come only with years of experience. For this reason, we greatly value the continuity of institutional knowledge of our current audit firm. This institutional knowledge greatly improves the auditor's ability to understand risks and evaluate accounting estimates and areas of judgment, and therefore is crucial to supporting our efforts to ensure that our operations and performance are appropriately reported to our investors and the external community. A lack of such continuity and institutional knowledge in the auditor would substantially increase the risk that audits will not be of the same high quality during the initial years of a new audit firm's engagement. This unnecessary risk is very much to the detriment of investors.

It is widely recognized that mandatory audit rotation would increase costs. We have no empirical data related to the incremental costs of mandatory audit firm rotation in the initial years, but we estimate that it would be more than the 20% indicated at the time of the 2003 GAO study. This is driven in part by our experience meeting SOX requirements, which we support, but whose implementation costs greatly exceeded estimates made at the time of adoption. Increased costs associated with audit firm rotation will arise primarily from the need for larger audit staffs in the initial years of engagement as the incoming audit team becomes familiar with the industry, operations and financials of a new client. There will also be significant disruption to the company's financial and operating personnel as additional time and effort is diverted from core responsibilities to interacting with, and providing institutional knowledge to the new auditors. We believe this additional time and effort could easily result in the need for adding incremental company finance staff, further increasing costs. It could also result in increased risk of accounting and reporting errors due to greater distraction during already tight financial reporting schedules.

[1] SEC Final Rule, Strengthening the Commission's Requirement Regarding Auditor Independence

In summary, we strongly believe the incremental costs and risks of mandatory audit firm rotation are substantial, while the asserted benefits are questionable. SOX has already introduced regulations that adequately address auditor independence. We have received no comments from investors questioning the independence of our auditors or calling for specifically for mandatory audit firm rotation. In fact, our shareholder voting results reflect 99% approval of our current auditors.

Our detailed responses to selected questions posed by the Board are included in the attached Appendix.

* * *

We hope that our comments are helpful to the Board in its deliberations. If you have any questions on the content of this letter, please contact Al Ziarnik, Assistant Comptroller, at (925) 842-5031.

Very truly yours,

Matthew J. Foehr

Appendix – Responses to Selected Questions

Question 1. *If the Board determined to move forward with development of a rotation proposal, what would be an appropriate term length?*

The PCAOB is not the appropriate body to determine a term length for audit engagements. We strongly believe that a company's Audit Committee, which is responsible for the appointment, compensation and oversight of the company's audit firm, is best placed to determine the appropriate term length and circumstances under which the audit firm should be rotated.

Question 2. *Should different term lengths for different kinds of engagements be considered? If so, what characteristics, such as client size or industry, should this differentiation be based on?*

The circumstances surrounding the engagement of an audit firm are unique to each company, irrespective of the company's size or industry. We believe that mandatory rotation of auditors is not applicable to any specific group of companies or form of engagement. Rotation should be at the discretion of each company's Audit Committee, which is appropriately positioned to evaluate the risks and benefits of the audit firm's rotation.

Question 3. *Does audit effectiveness vary over an auditor's tenure on a particular engagement? For example, are auditors either more or less effective at the beginning of a new client relationship? If there is a "learning curve" before auditors can become effective, generally how long is it, and does it vary significantly by client type?*

There is significant industry and company-specific knowledge and familiarity that auditors must attain in order to be effective and protect shareholder interests. This knowledge is even more pronounced for highly complex and global industries such as our own. Our experience with mandatory rotation of the lead audit partner demonstrates the significance of the learning curve. The incoming lead audit partner will spend significant overlapping time with the departing lead partner. This enables the new partner to become acquainted with Chevron personnel, policies, processes, and operations and finance functions. Even though the lead audit partner is supported by continuity of audit staff, this transition time is absolutely critical to ensuring the transfer of institutional knowledge, establishing key company contacts, and minimizing audit quality disruption. It also helps mitigate the impact of the partner change on company finance and operating personnel. In a situation where we were to rotate not just the Audit Partner, but the entire team, it would be multiple years before the new audit firm would be positioned to effectively audit Chevron.

Question 4. *Some have also suggested that, in addition to being less effective at the beginning of an engagement, an auditor may be less diligent toward the end of the allowable term. On the other hand, others have suggested that auditors would be more diligent towards the end of the allowable term out of concern about what the replacement auditor might find. Would auditors become more or less diligent towards the end of their term? Does the answer depend on the length of the term?*

The controls implemented as part of SOX sufficiently address auditor independence and mitigate the risk of decreased auditor diligence. The mandatory rotation of audit partners ensures that partners will continue to reassess the diligence and quality of the audit team's work. Each audit partner's professional reputation is at risk if he/she becomes less diligent and shortfalls are uncovered by his/her successor. Each audit firm's professional reputation is also at risk in the event of a decline in audit quality. We have therefore seen that audit firms will take additional measures to ensure that both a proper level of independence and a high quality audit is maintained. For example, our audit team rotates lead managers,

not just lead partners, approximately every five years. Turnover of lead managers is typically timed to avoid the interval when lead partners must rotate. Even under current rules, if the audit firm does become less diligent or less effective in its audits, the Audit Committee has the obligation and authority to determine if it is in shareholders' best interests to rotate audit firms.

As already discussed above in our response to Question 3, there is a steep learning curve that new auditors must climb with associated risks to a high quality audit in the initial years of a firm's tenure. We have no evidence to suggest auditors then become less diligent as time passes. We instead believe that auditors continue to increase their value to shareholders as they grow their experience in the energy industry and specifically on Chevron's account.

Question 6. *Should the Board consider requiring rotation for all issuer audits or just for some subset, such as audits of large issuers? Should the Board consider applying a rotation rule to some other subset of issuer audits? For example, are there reasons for applying a rotation requirement only to audits of companies in certain industries?*

As stated in our response to Question 2, the circumstances surrounding the engagement of an audit firm are unique to each company. We believe that mandatory rotation of auditors should not be applicable to any specific group of companies or form of engagement. Rotation should be at the discretion of each company's Audit Committee which is best positioned to serve the company's shareholder interests.

Question 7. *To what extent would a rotation requirement limit a company's choice of an auditor? Are there specific industries or regions in which a rotation requirement would present particular difficulties in identifying an auditor with the necessary skills and expertise? Is it likely that some smaller audit firms might decide to leave the public company audit market due to the level of uncertainty regarding their ongoing client portfolios?*

Integrated, multinational energy companies have unique requirements due to the complexity and global extent of the business. Only the "Big Four" audit firms have the industry-specific knowledge, global reach and organizational capabilities to audit our operations. In some cases, even these firms would need to establish new offices or affiliates to meet the company's needs in the event of mandatory rotation. A mid-tier or small auditing firm would not have the capabilities to serve a company as large and global as Chevron to a standard satisfactory to our Audit Committee or the external community. Mandatory audit firm rotation would also unnecessarily complicate our arrangements with the other Big Four firms for ongoing non-audit engagements.

Question 10. *Would rotation create unique challenges for audits of multinational companies? For voluntary rotations that have taken place, what have been the implementation and cost issues and how have they been managed?*

As a large multinational corporation, our audits extend beyond the United States. Audits are performed on our foreign operations by local auditors, the majority of which are affiliates of our audit firm. In many remote locations where we operate, our auditor has – over a number of years – developed the local audit staff and level of industry expertise to audit our operations. In many of our locations, the affiliate or local office is the only local auditor with any experience auditing the oil and gas industry. If forced to rotate auditors, it would be challenging to find an audit firm that has both the local presence and global expertise in the oil and gas industry for all the countries in which we operate. The incoming audit firm would require substantial time to develop new networks of international audit professionals and offices capable

of auditing our operations. Procuring a local license alone can take considerable time, which would further increase the length of time before a newly engaged audit firm would be fully effective in auditing our international operations.

Question 14. *Some have expressed concern that rotation would lead to "opinion shopping," or that in competing for new engagements firms would offer favorable treatment. Others have suggested that rotation could be an antidote to opinion shopping because companies would know that they could not stick with a firm promising favorable treatment forever. Would opinion shopping be more or less likely if rotation were required? If rotation limits auditor choice, could it at the same time increase opinion shopping?*

We believe that current audit regulations and oversight sufficiently ensure independent and high quality audits and prevent "opinion shopping." These existing oversight mechanisms, particularly those exercised through Audit Committee responsibilities, make mandatory audit rotation unnecessary.

Question 16. *Are there any requirements the Board should consider to mitigate any risks posed by rotation? For example, are there enhancements to firms' quality control systems that might address such risks?*

We believe the risks associated with mandatory audit rotation would not be easily or cost-effectively mitigated by introducing additional compensating controls. The suggested need for such compensating controls further increases the cost of compliance and therefore is not in the best interest of shareholders.

Question 17. *If the early years of an auditor-client relationship pose higher audit risks than later years, should the Board require firms to provide additional audit supervision and oversight in the first year or two of a new engagement? Should the Board impose such a requirement for auditor changes even if it does not further consider requiring audit firm rotation? If firms are accepting new clients but are unable to perform quality audits for them until several years have passed, should the Board require enhanced client acceptance procedures? What impact would additional requirements of this type have on audit costs?*

We agree that the early years would pose higher audit risks following auditor rotation, whether it be mandatory or voluntary rotation. Additional audit supervision would not alleviate the main risks of audit rotation as it does not address the loss of significant industry and institutional knowledge with the departing audit firm. A blanket requirement for additional audit supervision and oversight upon auditor rotation would only further increase a company's compliance costs, and not necessarily provide improved audit quality and associated benefits for shareholders. We believe it should be left to the Audit Committee to determine the most effective means of managing the increased risks based on the company's specific requirements and the incoming audit firm's expertise and staffing levels.

Question 20. *If the Board moved forward with development of a rotation proposal, should consideration be given to the recommendation for a cause restriction on the company's ability to remove an auditor before the end of a fixed term? Would such a provision be useful?*

Including a fixed-term provision would introduce a potential hindrance to the Audit Committee's oversight responsibilities. Per SOX requirements, the Audit Committee is responsible for auditor selection and oversight. If the Audit Committee were to determine that an audit firm was not appropriately diligent in its audit, under such a fixed-term provision the Committee would be forced to retain the underperforming audit firm, which effectively nullifies the Committee's oversight and authority to act in shareholders' best interests.

Question 21. *What other transition issues might arise in the first year of a rotation requirement? How should the Board address these issues?*

As highlighted throughout the points above, mandatory audit firm rotation would create tremendous disruption, likely depriving the investor community of high quality audits in the initial years and further burdening company finance and operating personnel who would be required to help transition the new auditors. We agree that, in certain circumstances, audit firm change may be necessary and in the best interest of a company's shareholders. However, such a decision needs to be carefully deliberated by individuals who understand the unique situation of a company and the resulting risks and benefits resulting from auditor change. We believe that the body best placed to make such a decision is the company's Audit Committee. A blanket regulation for mandatory audit firm rotation will likely degrade rather than enhance audit quality, will significantly increase compliance costs borne by the investor, and will likely result in more harm than benefit.