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December 14, 2011

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

RE: PCAOB Rulemaking Docket Matter No. 37, *Concept Release on Auditor Independence and Audit Firm Rotation*

Members of the Board:

Thank you for the opportunity to provide comments to the Board with respect to your recent *Concept Release on Auditor Independence and Audit Firm Rotation* (the Concept Release).

Rockwell Collins (the Company) is a pioneer in the development and deployment of innovative communication and aviation electronic solutions for both commercial and government applications. We have approximately 20,000 employees and revenue for our fiscal year ended September 30, 2011 was \$4.8 billion. With headquarters in Cedar Rapids, Iowa, we operate a global service and support network that crosses 27 countries.

Executive Summary

The Company and its Audit Committee are committed to ensuring that high quality financial statements are provided to investors and other stakeholders. The Company believes that procuring a high quality, independent audit of those financial statements is critical to ensuring investor confidence. Deloitte has been the lead provider of external audit services for the Company since 2001. Based upon the high audit quality and service provided by Deloitte, the Company and its Audit Committee have worked in recent years to consolidate statutory audits of all international subsidiaries with Deloitte. Our engagement of Deloitte on a world-wide basis has improved the quality of both the annual audit of the Company's financial statements and its internal controls.

Rockwell Collins and its Audit Committee are opposed to mandatory audit firm rotation. Any new regulation involves both costs and benefits, which must be carefully weighed. The main benefit associated with mandatory audit firm rotation, as explained by the PCAOB, is that increased competition and shorter engagement tenure could potentially enhance auditor independence. However, the PCAOB has offered little empirical evidence to support

this assertion. From our point of view, basing such a drastic proposal on inconclusive evidence presents substantial risks for issuers and the broader capital markets, including the following:

- **Decreased audit quality** – Consistent with numerous empirical studies, the Company believes that mandatory firm rotation is likely to decrease audit quality throughout the life of the engagement.
 - **Early years of the engagement** – The lack of knowledge possessed by a new audit firm regarding the client and the industry in which it operates presents a significant, negative impact on audit quality. Further, the complexity associated with large multi-national companies presents a specific challenge for a new auditor in building relationships and knowledge across its international network.
 - **Final years of the engagement** – Audit firm partners are likely to spend increased time on sales and marketing activities during the later years of the engagement as they seek to identify a replacement client. These incremental efforts are likely to distract the partner's attention from the task of auditing the current client, negatively impacting audit quality. Further, high talent audit staff members are likely to be rotated to new engagements and replaced by lower caliber staff members near the end of the engagement, further degrading audit quality.
 - **Throughout the engagement** – The increased audit staff layoffs and turnover that will result from mandatory firm rotation are likely to decrease the attractiveness of the audit profession and the quality of the talent employed.
- **Undermined Audit Committee authority** – Given their relationships with and supervisory responsibilities for both management and the auditor, the independent directors of the Audit Committee are best positioned to ensure that the Company's audit needs are met by its auditor.
- **Increased costs** – In the long-run, audit fees will likely increase as a result of mandatory firm rotation due to the incremental effort associated with learning the new client's risks, products, processes, controls and the industry environment in which it operates. Mandatory audit firm rotation will also impose incremental costs on Audit Committees and management as they evaluate potential replacement firms and spend large amounts of time training the new auditor.

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We suggest that, rather than mandating across the board auditor rotation, it would be more appropriate for the PCAOB to share the results of its full inspection reports with the Audit Committee of issuers whose audits were selected for review. In this regard, Audit Committees would have more information available, enabling them to exercise their judgment to terminate the incumbent auditor on engagements in which the PCAOB has substantiated a material failure by the auditor to maintain appropriate independence or professional skepticism.

Thank you for the opportunity to comment on this important subject. A more detailed explanation of the points raised in this letter is included in the Appendix below.

Sincerely,

/s/ Marsha A. Schulte

Marsha A. Schulte
Vice President, Finance and Controller
Rockwell Collins, Inc.

APPENDIX

Negative Impact on Audit Quality

The Company believes that mandatory firm rotation is likely to decrease audit quality throughout the life of the engagement while increasing costs.

Early years of the engagement

As discussed in the Concept Release, “[t]here are a number of studies on the relationship between auditor tenure and audit quality. Many, though not all, tend to support the view that engagements with short tenure are relatively riskier.”¹

The conclusion that audit quality suffers during the early years of the engagement, supported by the studies noted above, is consistent with the experience of some of the Company’s finance leaders, who themselves are former public company auditors. In their experience, the lack of institutional knowledge possessed by a new audit firm presents a significant, negative impact on audit quality during the early years of the engagement.

The Company also believes that mandatory firm rotation is likely to result in excessive focus on highly generalized areas of risk by new auditors. Given their lack of knowledge regarding the risks specific to the client and the industry in which it operates, audit procedures will likely be skewed towards generic risks and the “hot topic of the day,” with undue focus being placed on whatever is making headline news throughout corporate America. Excessive focus on these generalized emerging areas of risk will likely divert focus from areas of true company or industry specific risk that are more significant and deserve additional audit attention and procedures.

Further, the Company has experienced the challenge associated with the lead auditor coordinating the work of the member firms of its international network. As mentioned earlier, the Company has recently consolidated all international audit services with Deloitte. An outcome of this consolidation is improved audit quality across the globe. These improvements, however, do not come easily; it is clear from our experience that several audit cycles are required for the lead auditor to build effective relationships with the international network to ensure a high quality audit. Deloitte’s 2011 engagement plan includes the services of at least 12 partner firms from its international network to complete both statutory audits and the audit of the Company’s financial statements and internal controls. Using Deloitte to complete our statutory audits at non-U.S. subsidiaries has resulted in improvements in our control environment. We believe mandatory firm rotation would decrease audit quality in the early years of the engagement as it takes an extensive

¹ Concept Release, page 16

amount of time for a new auditor to build relationships and knowledge across its international network.

Finally, in an environment of mandated rotation, audit firms are likely to aggressively pursue new clients whose auditors have reached the end of their maximum term. Audit firms are likely to be highly motivated to secure new engagements, particularly in situations where they need to replace a client lost to mandatory firm rotation. Motivation to secure new clients, combined with a lack of knowledge of the company and industry, may result in audit bids that are unrealistically low for the first year of the new engagement. This situation could result in engagement staffing plans which are inconsistent with the goal of high audit quality.

Later years of the engagement

Mandatory audit firm rotation will result in disruptive transition periods. The current state process of audit partner rotation works well and provides the benefit of a “fresh set of eyes” without being overly disruptive. We utilize a similar rotation philosophy at Rockwell Collins in that we regularly rotate finance and other leaders amongst our different divisions. Our rotation approach, however, is well coordinated and balanced. Bringing in an entirely different audit firm without regard for continuity and ignoring the change management implications would be very disruptive, analogous to arbitrarily implementing a brand new ERP system every few years.

Further, the Concept Release fails to acknowledge that many financial reporting issues overlap fiscal years and require extensive up-front planning. For example, as a government contractor, we regularly enter into long-term contracts with our customers. A complex customer contract being negotiated today requires careful analysis of the revenue recognition implications that will occur in future years. Under the current state model of partner rotation, the new audit partner can “shadow” the outgoing audit partner in the final year of the engagement. In this regard, financial reporting issues that overlap fiscal years can be readily addressed on a real-time basis with both the incumbent partner and new audit partner participating in the discussion in a cost effective and timely manner. This approach would be cost prohibitive under a mandatory audit firm rotation model and would result in routine financial reporting decisions being unnecessarily debated over and over again by a constantly changing cast of characters.

Further, the outgoing audit firm will have decreased motivation to provide input on financial reporting issues that overlap fiscal years. A customer contract being negotiated by the issuer today that impacts next year’s financial statements is of less relevance to the outgoing audit firm.

Mandatory firm rotation will also introduce significant uncertainty into the professional future of public company auditors. As the end of the mandated maximum term approaches, staff will likely become increasingly distracted and concerned about how their future livelihood will be impacted by the loss of a key client. Partners are likely to spend increased time on sales and marketing activities as they seek to identify a new client to replace the audit fee stream lost due to mandatory firm rotation. Given public accounting partners' unique dual responsibilities for both sales and service delivery, an increased focus on marketing the firm's services to potential replacement clients is very likely to distract partner attention from the task of auditing the current client. The Company believes that stretching a partner's limited capacity to include identifying a new client is likely to negatively impact audit quality during the later years of the engagement.

The other members of the audit staff are likely to be similarly distracted. Their distraction is likely to be manifested in requests for transfer to engagement teams associated with new, high profile audit clients. New engagements are more likely to be viewed as attractive by audit staff members as they are more likely to provide longer-term employment security. This situation could lead to overall lower audit quality near the end of the engagement as high quality talent is rotated to new engagements, only to be replaced by lower caliber staff members during the "lame duck" period of the final audit year.

Throughout the life of the engagement

The Company is concerned that mandatory firm rotation may negatively impact the attractiveness of the audit profession, decreasing the quality of the talent employed in the profession. Audit firms today experience high staff turnover due in part to the demands of the profession. The increased volatility that will result from mandatory firm rotation is very likely to increase the prevalence of layoffs by the audit firms as it will be impossible to accurately forecast the number of audit hours to be secured through competitive bids in any given year. In some years, an individual firm may gain more audit hours than it lost to mandatory firm rotation, a situation which will result in a shortage of staff and potentially decreased audit quality. However, in other years, an individual firm may experience a significant decline in audit hours due to the loss of one or more major clients to mandatory firm rotation, combined with less new client wins than expected, thereby precipitating significant and unpredictable staff layoffs. The adverse impact from this volatility would likely be more pronounced for audit firms located in smaller markets, such as Cedar Rapids, Iowa.

Staff members would also be likely to spend far more time away from their home cities if mandatory firm rotation is enacted. The turnover in a firm's engagements precipitated by firm rotation will inevitably result in the excess staff from one office being required to travel

regularly to cities where a different office of the same firm experienced a shortage of staff. Volatility related to layoffs and increased travel is likely to make the audit profession less attractive, leading to more significant challenges in attracting and retaining high quality staff. This situation is unlikely to increase audit quality; rather, the Company believes that lower quality staff is likely to result in decreased audit quality throughout the life of the engagement. At a minimum, the volatility would most certainly contribute to increased audit costs.

Lack of Evidence in Support of Highly Disruptive Proposal

The concept release offers no evidence supporting the Board's claim that a lack of independence resulting from the potential perpetual audit fee stream is the root cause of audit failures. Basing the drastic mandatory audit rotation proposal on a combination of inconclusive evidence and conjecture does not seem prudent, especially considering the highly disruptive nature of the proposal and potential for decreased audit quality and increased costs.

In the Concept Release, the Board notes that "[p]reliminary analysis of [inspections] data appears to show no correlation between auditor tenure and number of comments in PCAOB inspection reports."² The Board also notes that "[i]ndependence is both a description of the relationship between auditor and client and the mindset with which the auditor must approach his or her work...One measure of this mindset is the auditor's ability to exercise 'professional skepticism,' which is described as 'an attitude that includes a questioning mind and a critical assessment of audit evidence.'"³ In other words, the Board acknowledges that independence is impacted by both the nature of the relationship with the client and the auditor's technical competence. The Board elaborates on this view in the Concept Release when they state "[a]udit failures can also reflect a lack of technical competence or experience, which may be exacerbated by staffing pressures or some other problem."⁴

The Board cites a series of audit failure examples in the Concept Release.⁵ The Company agrees that these examples represent failures by the auditor to employ appropriate levels of professional skepticism; however, we believe these situations may often be influenced by a lack of technical competence and critical thinking. The solutions proposed by the Board in the Concept Release fail to appropriately acknowledge the likely influence of insufficient technical competence on audit failures as defined by the Board.

² *Ibid.*

³ *Ibid.*, page 4

⁴ *Ibid.*, page 6

⁵ *Ibid.*, page 7

Chairman Doty's remarks upon issuance of the Concept Release provide another example of insufficient evidence being cited as justification for solutions proposed in the Concept Release. In those comments, and again during his address to the NASBA 104th Annual Meeting on October 24, Chairman Doty cites Glass Lewis research indicating that "more than 6,500 public companies, or nearly 52% of all public companies, voluntarily changed their auditors" between 2003 and 2006.⁶ On the surface, this data seems to imply that changing auditors is a relatively easy task. However, a closer look at the Glass Lewis study reveals the overwhelming influence of small companies on this data. For example, Glass Lewis notes that 85% of auditor changes which occurred in 2004 were by companies with less than \$100 million in revenue.⁷ The Company believes there is a fundamental difference between a small entity with revenues of less than \$100 million per year and a complex multi-national issuer that must comply with a wide variety of regulatory and financial reporting requirements in numerous jurisdictions across the globe. Further, the statistics cited by Chairman Doty fail to acknowledge the significant impact of other factors influencing auditor changes. For example, more than 20% of the auditor changes Glass Lewis identified in 2004 were driven by company mergers, audit firm mergers, or auditors resigning due to resource constraints or failure to meet SEC requirements for auditing public companies.⁸

The Company finds the lack of evidence supporting the Concept Release proposal to be very troubling. Given the significant changes to the public company audit environment resulting from the Sarbanes-Oxley reforms, we would expect the Board has numerous opportunities to conduct evidence-based research related to the resultant impacts on audit quality. In particular, a study regarding the impact that mandatory audit *partner* rotation has had on audit quality might be enlightening. Our experience is that partner rotation works well even though it does require some additional effort and cost. Further data regarding the impact on audit quality and cost-benefit considerations associated with mandatory partner rotation would provide compelling fact-based evidence that would contribute to a rational discussion and debate about audit quality; the conjecture and unsubstantiated opinion on which the Concept Release is based does not contribute to such a discussion and debate.

In his remarks upon issuance of the Concept Release, Mr. Goelzer notes that "[i]t may be possible to draw relevant conclusions about the impact of tenure on audit quality from our

⁶ Chairman Doty's remarks upon issuance of the Concept Release on August 16, 2011 accessed on November 15, 2011 from http://pcaobus.org/News/Speech/Pages/08162011_DotyStatement.aspx and Chairman Doty's address to the NASBA 104th Annual Meeting on October 24, 2011 accessed on November 15, 2011 from http://pcaobus.org/News/Speech/Pages/10242011_DotyNASBA.aspx

⁷ *Auditor Turnover Gains Momentum in 2004* by Glass Lewis & Company dated February 15, 2005 accessed on November 15, 2011 from http://www.glasslewis.com/downloads/sampleresearch/TrendReport_AuditorTurnover.pdf, page 3

⁸ *Ibid.*, from data on pages 12 and 13

inspections records, but the necessary analytical work has not yet been done.”⁹ We strongly encourage the Board to undertake an evidence-based study of the issues contributing to audit failures and propose responses that are proportional to any deficiencies identified.

Mandatory Firm Rotation Undermines Audit Committee Role and Assumes All Accounting Firms or Engagements are Equal

The Sarbanes-Oxley Act of 2002 empowered public company Audit Committees with specific responsibilities regarding the external audit. Mandatory audit firm rotation would undermine the Audit Committee’s ability to analyze differences amongst the firms and to select the most qualified provider. The Company’s Audit Committee takes very seriously its responsibility for assessing the independence, objectivity and professional skepticism maintained by the Company’s audit firm. Through this annual assessment and performance evaluation, the Audit Committee gains comfort that Deloitte has maintained its independence and is best positioned to provide audit services on behalf of the Company and its shareowners. If the Audit Committee was unable to gain sufficient comfort with regard to Deloitte’s independence or expertise, it would solicit bids from other qualified audit firms.

The Concept Release implies that audit services are a simplistic commodity whereby Audit Firm A can easily be replaced with Audit Firm B. The Company has had experience with all of the Big Four firms on a variety of projects. Further, the Company has made various acquisitions in the past and has overseen the transition of audit work from the legacy auditor of the target company over to our auditor, Deloitte. As a result of these experiences, the Company believes there are indeed differences amongst the Big Four accounting firms and that mandatory audit firm rotation would have a negative impact on the level of industry specialization amongst auditors.

Our Company operates in the Aerospace and Defense (A&D) industry and requires an audit firm that understands the various regulations and risks specific to our industry. Not only do auditors experience a ‘new client’ learning curve, but there is clearly an industry learning curve as well. Certain audit firms have a greater degree of institutional knowledge about the A&D industry than others. Mandatory audit firm rotation is likely to force audit firms to increasingly become ‘generalists,’ thus disrupting the audit firm’s ability to retain their industry specialization.

Given their management oversight responsibilities with regard to financial reporting, internal controls and the internal audit function, the Audit Committee consults regularly with management regarding specific risks facing the enterprise. Based upon the knowledge

⁹ Daniel L. Goelzer’s remarks upon issuance of the Concept Release on August 16, 2011 accessed on November 15, 2011 from http://pcaobus.org/News/Speech/Pages/08162011_GoelzerStatement.aspx

gained through these interactions, the Audit Committee addresses its specific concerns with Deloitte to gain comfort regarding their ability to effectively address those risks. The independent directors of the Audit Committee are best positioned to ensure that the audit needs of the Company are appropriately met by its auditor.

An Alternative

Given the significant threat to audit quality the Company believes is inherent in the Board's proposal, we believe an alternative approach is more appropriate. This approach would be proportional in that it would not impose disruptive change on all issuers and auditors, risking significant and widely recognized concerns regarding decreased audit quality resulting from mandatory firm rotation. This alternative approach would also preserve the Audit Committee's role to independently appoint external audit firms.

The Company would support changes requiring the PCAOB to share full inspection reports regarding its examinations of the Company's audits with the Audit Committee. Sharing PCAOB inspectors' views regarding an audit firm's work would be of great value to the Audit Committee's efforts to assess the quality of the auditors' work. By sharing these inspection reports, Audit Committees will be able to properly evaluate circumstances where a PCAOB inspection reveals specific situations of an inappropriate lack of auditor independence or of professional skepticism.

The Board has not made a convincing argument that auditor independence issues are pervasive or are definitively caused by the potential for a long-term income stream. Rather, the Concept Release notes that "the Board continues to find instances in which **it appears** that auditors did not approach some aspect of the audit with the required independence, objectivity and professional skepticism [emphasis added]."¹⁰ Chairman Doty's Keynote Address to the 43rd Annual Securities Regulation Institute on November 10, 2011 noted that PCAOB inspections "have reviewed significant aspects of approximately 3,000 engagements of such firms and discovered and analyzed hundreds of cases involving what they determined to rise to the level of an audit failure. Sometimes, inspectors can trace an audit failure to a competence issue, such as in the design of the audit methodology or in relation to a new or complex accounting standard."¹¹ While the Company acknowledges that this failure rate is unacceptable, it is clear from these remarks that the vast majority of auditors are maintaining appropriate levels of independence and professional skepticism, effectively fulfilling their responsibilities to the investor community.

¹⁰ Concept Release, page 2

¹¹ Chairman Doty's Keynote Address to the 43rd Annual Securities Regulation Institute on November 10, 2011 accessed on November 15, 2011 from http://pcaobus.org/News/Speech/Pages/11102011_DotyKeynote.aspx

The Concept release also states that “the Board may be looking at the most error-prone situations. The root causes of audit failures are complex and vary in nature and continue to be explored by the Board. The Board plans to deepen its understanding of root causes in upcoming inspection seasons.”¹² The Board’s *Report on the PCAOB’s 2004, 2005, 2006, and 2007 Inspections of Domestic Annually Inspected Firms* noted that “[t]he selection of issuer audits to inspect has been influenced by the evaluation of the risk of material misstatement of financial statements. Risk may be related to characteristics of the particular issuer or its industry; the audit issues likely to be encountered; firm-, practice office-, or individual partner-level considerations; prior inspection results; or other factors.”¹³ The risk based approach to inspection utilized by the PCAOB is rational in that it increases the likelihood that significant audit failures are identified, but it also increases the likelihood that audit failures detected by PCAOB inspectors are the result of insufficient technical competence of an audit firm, as opposed to a lack of independence and professional skepticism.

Limiting rotation to the largest issuers is not an appropriate alternative to mandatory firm rotation for all issuers. The largest issuers tend to be the most complex. Given the potential for negative impact on audit quality and the unbalanced cost-benefit considerations discussed above, focusing mandatory firm rotation on the largest issuers would not be appropriate.

The Company believes sharing PCAOB inspection reports with issuers will help Audit Committees properly react to specific circumstances in which auditors failed to execute their responsibilities with appropriate levels of independence and professional skepticism. In situations such as this, the Audit Committee could evaluate whether rotation of the auditor is appropriate.

This alternative represents a proportional response to the Board’s concerns regarding auditor independence. Further, auditor termination by an Audit Committee following findings of a lack of independence or appropriate professional skepticism would likely be more effective in focusing firms on the underlying issues than the PCAOB’s proposed mandatory firm rotation proposal. Under this alternative, the reputational damage to the displaced auditor would be clear and the replacement auditor would have the opportunity to retain the new client on a long-term basis only if they provide effective client service while maintaining appropriate levels of independence and professional skepticism.

¹² Concept Release, page 6

¹³ PCAOB *Report on the PCAOB’s 2004, 2005, 2006, and 2007 Inspections of Domestic Annually Inspected Firms* dated December 5, 2008 accessed on November 15, 2011 from http://pcaobus.org/Inspections/Documents/2008_12-05_Release_2008-008.pdf, page 6