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Mastering the PCAOB's New Extensive Reporting Mandate on Firm Activities

Preparing Now to Meet Annual and Special Disclosure Requirements

A Live 110-Minute Teleconference/Webinar with Interactive Q&A

Today's panel features:

Mary Peters, Assistant General Counsel, **Public Company Accounting Oversight Board**, Washington, D.C.

Barry Smith, **Accounting Consultant**, Philadelphia

Walter McNairy, Member and Director of SEC Services, **Dixon Hughes**, Raleigh, N.C.

Tuesday, October 27, 2009

The conference begins at:

1 pm Eastern

12 pm Central

11 am Mountain

10 am Pacific

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Mastering The PCAOB's New Extensive Reporting Mandate On Firm Activities Webinar

Oct. 27, 2009

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Caveat

The views expressed in this presentation are my own and do not necessarily reflect the views of the Board, its members or staff. Therefore, unless it is clear that the Board has authorized the statement, you should not attribute it to the Board or staff.

Introduction Of Reporting Rules

- ❑ Adopted by PCAOB on June 10, 2008
- ❑ Approved by SEC on Aug. 13, 2009
- ❑ Effective Dec. 31, 2009
- ❑ Require firms to report certain information annually on Form 2
- ❑ Require special reporting regarding certain specified events within 30 days of the event on Form 3

Statutory Requirement Of Periodic Reporting

- ❑ Sect. 102(d) of the Sarbanes-Oxley Act ("Act"), 15 U.S.C. § 7212(d), requires annual reporting by registered firms and permits the Board to require special reporting
- ❑ Information required by the Act includes updates to information reported in a firm's application for registration (Form 1) and additional information that the Board or the Securities and Exchange Commission deems necessary or appropriate in the public interest or for the protection of investors
- ❑ To the extent that the Board identifies additional reporting requirements that are necessary or appropriate in the public interest or for the protection of investors, the Board may propose and adopt them at any time
 - Recommendations made by the U.S. Department of the Treasury's Advisory Committee on the Auditing Profession in October 2008 relating to transparency of public accounting firms and specific disclosures by registered firms (available at <http://www.treasury.gov/offices/domestic-finance/acap/>)

Purposes Of The Reporting Requirements

□ Purposes

- To keep the Board's records current regarding basic matters
- To facilitate analysis and planning related to the Board's inspection responsibilities and to inform other Board functions
- To bring to the Board's attention circumstances or events that may merit follow-up through the Board's inspection process or its enforcement process
- To provide the public more information about registered firms

New Web-based System For Registration And Reporting

- New Web-based system will be implemented in late 2009
 - All forms for both registration and reporting must be filed electronically in the system
 - Technical specifications
 - To file forms, registered firms must access the Board's system and will need Internet Explorer 6.0 and later or Firefox 2.0 and later
 - Registered firms may complete Forms 2 and 3 as Web forms or in XML
 - Form 4 may be completed only as a Web form
 - Exhibits required to be included with any form must be submitted in PDF, GIF or JPEG format
 - Forms available to public soon after being filed
 - Forms organized by firm and in chronological order
 - Electronic mechanism for firms to amend forms to correct information previously reported
 - Availability of confidential treatment limited for new forms

Confidential Treatment

- The new forms (Forms 2, 3, and 4) identify certain categories of information for which a firm may not request confidential treatment
 - Limitation reflects determination by Board that for these certain categories of information, there is no genuine possibility that the information could include information that is proprietary or otherwise protected from disclosure by applicable law

- New requirements regarding process for requesting confidential treatment
 - Representation by firm that information has not otherwise been publicly disclosed; and
 - Either:
 - Detailed explanation of grounds on which the information is considered proprietary, or
 - Detailed explanation of basis for asserting the information is protected by law from public disclosure and a copy of the specific provision of law
 - Failure to provide required support constitutes sufficient grounds for denial of request

Confidential Treatment (Cont.)

- Information for which a firm may not request confidential treatment
 - Information identifying the firm, contact persons and office locations
 - Period covered by annual report
 - General information about the firm's practice
 - For U.S. firms, the percentage of the firm's annual billings attributable to certain broad categories of services provided to issuers
 - Identity of the firm's issuer clients
 - Basic information about whether a firm is a member of any network or affiliation related to its audit practice
 - Identity of any other firm acquired by the firm
 - Affirmation of the firm's statutorily required consent to cooperate with the Board
 - Identity of an issuer concerning which the firm has withdrawn an audit report and the date of the audit report
 - Changes in authorization to engage in the business of auditing or accounting

Annual Reporting – Form 2

Form 2 includes:

- ❑ General information concerning the firm
- ❑ Audit clients and audit reports
- ❑ Offices and affiliations
- ❑ Personnel
- ❑ Certain relationships
- ❑ Acquisitions
- ❑ Affirmation of consent

Annual Reporting – Form 2 (Cont.)

- Reporting period is the 12-month period from April 1 through March 31

- Report is due by June 30

- Annual fee is due by July 31
 - Fee amount for 2010 has not yet been announced by the Board

Special Reporting – Form 3

Form 3 triggering events and disclosures include:

- ❑ Name change
- ❑ Audit reports (withdrew a report or consent, or crossed 100-issuer threshold)
- ❑ Certain legal proceedings
- ❑ Bankruptcy
- ❑ Certain relationships
- ❑ Licenses and certifications
- ❑ Changes in the firm's Board contact person

Special Reporting – Form 3 (Cont.)

- ❑ Form 3 must be filed within 30 days of the triggering event
- ❑ Form 3 to “bring current” certain events that have occurred since firm’s filing of Form 1 due by Feb. 1, 2010

Succeeding To A Predecessor Firm's Registration Status – Form 4

- ❑ Adopted July 28, 2008
- ❑ Approved by SEC Aug. 13, 2009
- ❑ Effective Dec. 31, 2009
- ❑ Allow firms whose structure has changed to retain registration status under two scenarios:
 - A registered firm changes its legal form of organization or jurisdiction in which it operates
 - A registered firm is acquired by an unregistered firm or merges with another firm to create a new legal entity

Succeeding To A Predecessor Firm's Registration Status – Form 4 (Cont.)

- The rules provide for:
 - A form to be filed (Form 4)
 - Within 14 days after the event
 - With certain representations
- Continuity of registration status
 - Continuity of registration is automatic for firm without the need for Board action, if certain conditions are met
 - If some, but not all, conditions are met, firm may be temporarily registered for up to 90 days
- If deadline for filing Form 4 is not met, the registration process using Form 1 may be required along with Board action
- If firm has had applicable transaction since firm filed its Form 1, Form 4 must be filed by Jan. 14, 2010 or else a new Form 1 may be required

Guidance Issued By The Board Re: Reporting Rules And Succeeding To Registration

- Closer to the effective date, the Board will publish additional guidance for registered firms concerning use of the Web-based filing system and concerning compliance with the substantive reporting requirements

- Detailed information concerning the substantive requirements is currently available in the Board's adopting releases, at the following links:
 - Periodic Reporting by Registered Public Accounting Firms
http://www.pcaobus.org/Rules/Docket_019/index.aspx
 - Succeeding to the Registration Status of a Predecessor Firm
http://www.pcaobus.org/Rules/Docket_020/index.aspx

Pros, Cons Of Reporting By Registered Firm

Pros

- If are no reportable events, registered firm could use reporting as a positive marketing tool
- Timely and transparent reporting for use by public
- Places similar reporting responsibility on registered firms as publicly traded companies
- Puts all firms on a level playing field

Cons

- System implementation and modifications to comply with timeliness of information
- Reporting burden
- Additional ongoing costs
- If firm has reportable events, could be used as a negative marketing tool by competing firms

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Data Gathering Systems And Quality Control

- Re-evaluate quality control systems and procedures, and real-time information-gathering systems
 - Appoint one partner in the firm to take charge of periodic reporting with the PCAOB
 - Cut-off date of March 31 vs. the firm's normal reporting date
 - Centralization of required information (inspection, clarification, 14-day reporting requirement)
 - Firm requirements for issuing reports for registered companies
 - Monitoring client additions, terminations, withdrawals
 - Monitoring ongoing compliance sufficiently to alert as to reporting requirements
 - Procedures to ensure compliance with foreign firm law prohibitions
 - Systems to indentify/agreements with other firms as to “playing a substantial role” in a registered company's audit and accumulation of data
 - Procedures in “due diligence” of an acquisition of a firm

Data Gathering Systems And Quality Control (Cont.

Form 3

- Reevaluate firm's professional quality control policies and procedures and real-time systems
 - System for gathering reporting events that require filing (note: for purposes of Form 3, the firm is aware of relevant facts on the date “any partner, shareholder, principal owner or member of the Firm first becomes aware of the facts”)

Potential Confidential Treatment Request

- Bear in mind: PCAOB hasn't publicly identified any information it considers confidential *per se*
- 2003 release on registration rules, and releases on annual and special reporting rules, do address one consideration for making a request to treat information as confidential
 - That is, non-U.S. firms may be subject to domestic laws that treat information as confidential that the U.S. wouldn't
 - E.g. European data protection laws that restrict type of information a company can divulge about employees
- One possible argument: Information to be divulged in PCAOB report is also part of court proceeding that has been filed under seal

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Form 2 Reporting Scenarios

- Firm: (a) audits issuers, (b) plays a substantial role in issuer audits, and (c) audits broker-dealers
 - Report issuers only
 - If no (a), report (b) only
 - If no (a) and (b), report (c) only
- Firm issued consent for a former client
 - If firm also issued an audit report during the reporting period, do not report
 - If firm did not issue an audit report during the reporting period, all such consents must be reported
- Firm maintains a database of fees charged to issuer clients that correspond to the proxy reporting requirements – those fees may be used
- Firm compiles proxy fee information only for periodic PCAOB inspection – firm may use fees billed during the reporting period

Common Scenarios – Form 3

- New partner is admitted to the firm, and background check reveals partner is currently under an SEC order denying the privilege to practice before the SEC
- Firm engages another CPA firm to perform inventory observation, and a partner in that CPA firm is currently under a PCAOB order suspending him from being an associated person of a registered public accounting firm
- Firm has become subject to an AICPA disciplinary proceeding arising out of a peer review
- Partner has become subject to an AICPA disciplinary proceeding relating to an ethics violation
 - Matter related to a public company audit
 - Matter related to a private company audit, but partner worked 10 hours on a public company audit
 - Matter related to private company audit; partner does not audit public companies
 - Matter related to any professional services

Common Scenarios – Form 3 (Cont.)

- Firm has had its license revoked to practice in the state of New York
- Firm has obtained a new client in California and has obtained a license to practice in California
- Manager is charged with obstruction of justice and is a defendant in a criminal proceeding
 - Worked on a public company audit for at least 10 hours
 - Never has worked on public company
- Partner inappropriately held himself out as a CPA in North Carolina and was subject to a disciplinary proceeding by the state CPA board
 - NC services performed were for a public company audit
 - NC services performed were for a non-public company, and partner worked on a public company audit for at least 10 hours
 - NC services performed were for a non-public company, and partner never has worked on a public company
- Firm's primary contact with the PCAOB has a new fax number

Common Scenarios – Form 3 (Cont.)

- Partner gets a speeding ticket
- Partner involved in a divorce
- Civil suit is filed against partner
- One of the firm's key SEC partners has been terminated by the firm
- Partner is licensed in a new state

Common Scenarios – Form 3 (Cont.)

- Firm is being sued by client
- Client files for bankruptcy
- Firm has received a subpoena for its workpapers on an audit for a client who is being investigated by a regulatory body
- Going concern opinion issued on a public company client
- Relationship with a public company client is terminated by the firm
- Firm refuses to consent for a former client

Form 3 Initial Reporting

Since the initial firm registration on Form 1, the firm:

- Obtained licenses to practice in 10 new states
- Changed its legal name
- Changed the business mailing address of the firm's primary contact with the board
- Has a partner who is currently subject to a disciplinary investigation by a state CPA board; proceeding is pending
 - Matter related to a public company audit
 - Matter related to a private company audit, but partner worked 10 hours on a public company audit
 - Matter related to private company audit; partner does not audit public companies

Form 3 Initial Reporting (Cont.)

- Has a partner who was subject to a disciplinary action by a state CPA board and had his license suspended – proceeding is complete:
 - Matter related to a public company audit
 - Matter related to a private company audit, but partner worked 10 hours on a public company audit
 - Matter related to private company audit; partner does not audit public companies

Action Steps

- Review the requirements of the new rules, both Form 2 and Form 3
- Communicate internally to key parties as to the new requirements
 - CEO
 - Management/executive committee
 - Director of HR
 - In-house or outside legal counsel
 - Compliance officer
 - All partners and managers in the firm
- Establish policies and procedures/protocol for reporting Form 3 events
- Determine Form 3 reportable items (as noted in General Instruction 4 to Form 3) that will need to be made within 30 days of the effective date of the new rules (i.e., **Feb. 1, 2010!**)

Action Steps (Cont.)

- Review internal accounting system information and determine a plan for capturing fees on issuer clients, using the four fee buckets required by Form 2
- Determine reporting period to be used (firm year-end or March 31)
- Maintain filing system for manually signed copies of Form 2 and Form 3 (seven-year retention period)
- Budget for PCAOB fee (once determined) and communicate to firm leadership

Action Steps For Smaller Firms

Action Steps

- Review the requirements of the new rules, both Form 2 and Form 3
- Communicate internally to key parties as to the new requirements
 - CEO
 - Management/executive committee
 - Director of HR
 - In-house or outside legal counsel
 - Compliance officer
 - All partners and managers in the firm
- Establish policies and procedures/protocol for reporting Form 3 events
- Determine Form 3 reportable items (as noted in General Instruction 4 to Form 3) that will need to be made within 30 days of the effective date of the new rules (i.e., **Feb. 1, 2010!**)

Action Steps (Cont.)

- Review internal accounting system information and determine a plan for capturing fees on issuer clients, using the four fee buckets required by Form 2
- Determine reporting period to be used (firm year-end or March 31)
- Maintain filing system for manually signed copies of Form 2 and Form 3 (seven-year retention period)
- Budget for PCAOB fee (once determined) and communicate to firm leadership