

conclusions with respect to the proposed rule change.

#### IV. Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the proposed rule change. In particular, the Commission invites the written views of interested persons concerning whether the proposed rule change is consistent with the Exchange Act and the rules thereunder.

Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.<sup>45</sup>

Interested persons are invited to submit written data, views, and arguments regarding whether the proposed rule change should be approved or disapproved by October 13, 2021. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by October 19, 2021. Comments may be submitted by any of the following methods:

##### Electronic Comments

- Use the Commission's internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2021-016 on the subject line.

##### Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2021-016. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (<http://www.sec.gov/>

[rules/sro.shtml](#)). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-FINRA-2021-016 and should be submitted on or before October 13, 2021. If comments are received, any rebuttal comments should be submitted on or before October 19, 2021.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>46</sup>

**J. Matthew DeLesDernier,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-93112; File No. PCAOB-2021-01]

### Public Company Accounting Oversight Board; Notice of Filing of Proposed Rule on Board Determinations Under the Holding Foreign Companies Accountable Act

September 23, 2021.

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), notice is hereby given that on September 23, 2021, the Public Company Accounting Oversight Board (the "Board" or "PCAOB") filed with the Securities and Exchange Commission (the "Commission" or "SEC") the proposed rule described in

items I and II below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed rule from interested persons.

#### I. Board's Statement of the Terms of Substance of the Proposed Rule

On September 22, 2021, the Board adopted PCAOB Rule 6100, *Board Determinations Under the Holding Foreign Companies Accountable Act* (the "proposed rule"). The text of the proposed rule appears in Exhibit A to the SEC Filing Form 19b-4 and is available on the Board's website at <https://pcaobus.org/about/rules-rulemaking/rulemaking-dockets/docket-048-proposed-rule-governing-board-determinations-under-holding-foreign-companies-accountable-act> and at the Commission's Public Reference Room.

#### II. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule

In its filing with the Commission, the Board included statements concerning the purpose of, and basis for, the proposed rule and discussed comments it received on the proposed rule. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in Sections A, B, C, and D below, of the most significant aspects of such statements. In addition, the Board is requesting that the Commission determine that Section 103(a)(3)(C) of the Act does not apply to the proposed rule. The Board's conclusion in this regard is set forth in Section D.

##### A. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule

###### (a) Purpose

The Act mandates that the Board inspect registered public accounting firms and investigate possible statutory, rule, and professional standards violations committed by those firms and their associated persons. That mandate applies with equal force to the Board's oversight of registered firms in the United States and in foreign jurisdictions.

Over the course of more than a decade, the Board has worked effectively with authorities in foreign jurisdictions to fulfill its mandate to oversee registered firms located outside the United States. With rare exceptions, foreign audit regulators have cooperated with the Board and allowed it to exercise its oversight authority as it relates to registered firms located within

<sup>45</sup> Section 19(b)(2) of the Exchange Act, as amended by the Securities Acts Amendments of 1975, Public Law 94-29, 89 Stat. 97 (1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Acts Amendments of 1975, Report of the Senate Committee on Banking, Housing and Urban Affairs to Accompany S. 249, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

<sup>46</sup> 17 CFR 200.30-3(a)(12); 17 CFR 200.30-3(a)(57).

their respective jurisdictions. The norms of international comity have guided those efforts and allowed the Board to work cooperatively across borders, to resolve conflicts of law, and to overcome other potential obstacles. The Board benefits greatly from cross-border cooperation with its international counterparts and has built constructive relationships that facilitate meaningful oversight. Authorities in a limited number of foreign jurisdictions, however, have taken positions that deny the Board the access it needs to conduct its mandated oversight activities.

Recognizing the ongoing obstacles to Board inspections and investigations in certain foreign jurisdictions, Congress enacted the Holding Foreign Companies Accountable Act (“HFCAA”).<sup>1</sup> The HFCAA requires that the Board determine whether it is unable to inspect or investigate completely registered public accounting firms located in a foreign jurisdiction because of a position taken by one or more authorities in that jurisdiction. The HFCAA, among other things, also mandates that, after the Board makes such a determination, the Commission shall require covered issuers<sup>2</sup> who retain such firms to make certain disclosures in their annual reports and, eventually, if certain conditions persist, shall prohibit trading in those issuers’ securities.<sup>3</sup>

Following public comment, the Board adopted the proposed rule, with some modifications after consideration of comments, to establish a framework for the Board to make its determinations under the HFCAA. The proposed rule establishes the manner of the Board’s determinations; the factors the Board will evaluate and the documents and information it will consider when assessing whether a determination is warranted; the form, public availability, effective date, and duration of such determinations; and the process by which the Board will reaffirm, modify, or vacate any such determinations.

## (b) Statutory Basis

The statutory basis for the proposed rule is Title I of the Act.

<sup>1</sup> Public Law 116–222, 134 Stat. 1063 (Dec. 18, 2020).

<sup>2</sup> See HFCAA § 2(i)(1)(A), 15 U.S.C. 7214(i)(1)(A) (defining “covered issuer”). An “issuer,” as that term is used here, is distinct from a “covered issuer,” and is defined in Section 2(a)(7) of the Act.

<sup>3</sup> See generally Holding Foreign Companies Accountable Act Disclosure, SEC Exchange Act Release No. 91364 (Mar. 18, 2021).

## B. Board’s Statement on Burden on Competition

Not applicable. The Board’s consideration of the economic impacts of the proposed rule is discussed in Section D below.

## C. Board’s Statement on Comments on the Proposed Rule Received From Members, Participants or Others

### Rulemaking History

On May 13, 2021, the Board proposed a new rule that would establish a framework for the Board’s determinations under the HFCAA.<sup>4</sup> The Board received eight comments on the proposal from commenters across a range of affiliations.<sup>5</sup> Commenters generally noted that the Board’s statutorily mandated oversight activities—including the Board inspections and investigations referenced in the HFCAA—promote audit quality and enhance the quality of financial reporting, which serve to protect investors and further the public interest. The proposed rule is informed by the comments received. The proposed rule also takes into account observations based on PCAOB oversight activities.

### Background

The Board’s Oversight of Non-U.S. Registered Public Accounting Firms Through Board Inspections and Investigations

Section 102 of the Act prohibits public accounting firms that are not registered with the Board from preparing or issuing, or from participating in the preparation or issuance of, audit reports with respect to issuers, brokers, or dealers.<sup>6</sup> Implementing this prohibition, PCAOB Rule 2100, *Registration Requirements for Public Accounting Firms*, provides that each public accounting firm that prepares or issues an audit report with

<sup>4</sup> See PCAOB Rel. No. 2021–001, Proposed Rule Governing Board Determinations Under the Holding Foreign Companies Accountable Act (May 13, 2021).

<sup>5</sup> The comment letters on the proposal are available on the Board’s website in Rulemaking Docket No. 048, available at <https://pcaobus.org/about/rules-rulemaking/rulemaking-dockets/docket-048-proposed-rule-governing-board-determinations-under-holding-foreign-companies-accountable-act>. During the comment period, Board members and staff discussed the proposal during a webinar for investors on international issues, a transcript of which also is available in Rulemaking Docket No. 048.

<sup>6</sup> See Section 102(a) of the Act; see also Section 2(a)(7) of the Act & PCAOB Rule 1001(i)(iii) (defining “issuer”); Section 110(3) of the Act & PCAOB Rule 1001(b)(iii) (defining “broker”); Section 110(4) of the Act & PCAOB Rule 1001(d)(iii) (defining “dealer”).

respect to an issuer, broker, or dealer, or plays a substantial role in the preparation or furnishing of such a report, must be registered with the Board.<sup>7</sup>

These provisions apply equally to U.S. and non-U.S. public accounting firms. Section 106 of the Act provides that any non-U.S. public accounting firm that prepares or furnishes an audit report with respect to an issuer, broker, or dealer is subject to the Act and to the Board’s rules “in the same manner and to the same extent” as a U.S. public accounting firm.<sup>8</sup> Therefore, non-U.S. firms issuing such reports must register with the Board. Section 106 of the Act further authorizes the Board to require non-U.S. firms that do not issue such reports but that play a substantial role in the preparation or furnishing of such reports to register with the Board,<sup>9</sup> and the Board exercised that authority when it adopted Rule 2100.<sup>10</sup>

Thus, by virtue of Section 106 of the Act and Rule 2100, non-U.S. firms are subject to the same registration requirements as U.S. firms, and, once registered, they are subject to the same oversight as U.S. firms. This oversight includes Board inspections at mandated regular intervals and Board investigations.

### The Board’s Inspection Mandate

The Act mandates that the Board administer a continuing program of inspections that assesses registered firms’ and their associated persons’ compliance with the Act, the rules of the Board, the rules of the Commission, and professional standards in connection with the performance of audits, the issuance of audit reports, and related matters involving issuers.<sup>11</sup>

<sup>7</sup> See PCAOB Rule 2100; see also PCAOB Rule 1001(p)(ii) (defining “play a substantial role in the preparation or furnishing of an audit report”).

<sup>8</sup> Section 106(a)(1) of the Act.

<sup>9</sup> See Section 106(a)(2) of the Act.

<sup>10</sup> See PCAOB Rule 2100. Section 106(c) of the Act allows the Board, subject to Commission approval, to exempt a non-U.S. firm or any class of such firms from any provision of the Act or the Board’s rules, upon a determination that doing so is necessary or appropriate in the public interest or for the protection of investors. In connection with the launch of its oversight system in 2003, the Board received numerous requests that non-U.S. firms be exempted from the Board’s oversight requirements, but the Board declined to adopt any such exemptions, finding such exemptions to be inconsistent with its mandate to protect investors. See, e.g., *Registration System for Public Accounting Firms*, PCAOB Rel. No. 2003–007, at 13, 17–20 (May 6, 2003); see also, e.g., *Final Rule Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms*, PCAOB Rel. No. 2009–003, at 9 n.23 (June 25, 2009).

<sup>11</sup> See Section 104(a)(1) of the Act; see also Section 101(c)(3) of the Act; PCAOB Rule 4000(a), *General*. The Act also permits the Board to

Board inspections are the Board's "primary tool of oversight."<sup>12</sup>

In accordance with the Act, and as set forth in the Board's rules, the Board periodically inspects the audits of registered public accounting firms.<sup>13</sup> Board inspections must be performed annually with respect to each registered firm that regularly provides audit reports for more than 100 issuers, and at least triennially with respect to each registered firm that regularly provides audit reports for 100 or fewer issuers.<sup>14</sup> The Board also may conduct special inspections on its own initiative or at the Commission's request.<sup>15</sup>

During an inspection, the Board reviews audit engagements "selected by the Board."<sup>16</sup> The Board also evaluates the sufficiency of the firm's quality control system (and the documentation and communication of that system), and may perform other testing of the firm's audit, supervisory, and quality control procedures as deemed necessary or appropriate in light of the purpose of the inspection and the responsibilities of the Board.<sup>17</sup>

To conduct an inspection, the Board must obtain documents and information from the firm and its associated persons, and when the Board requests such documents or information, registered firms and their associated persons must comply. In this regard, the Act provides that a firm's cooperation in and

compliance with document requests made in furtherance of the Board's authority and responsibilities under the Act are a condition to the continuing effectiveness of the firm's registration with the Board.<sup>18</sup> Furthermore, PCAOB Rule 4006, *Duty to Cooperate With Inspectors*, imposes on registered firms and their associated persons a duty to cooperate with PCAOB inspectors, which includes complying with requests for access to, and the ability to copy, any record in their possession, custody, or control, and with requests for information by oral interviews, written responses, or otherwise.<sup>19</sup>

#### The Board's Investigation Mandate

The Act also authorizes the Board to conduct investigations (and, relatedly, disciplinary proceedings) with respect to registered firms and their associated persons.<sup>20</sup> The Board may investigate any act, practice, or omission to act by a registered firm or associated person that may violate the Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under the Act, or professional standards, regardless of how the act, practice, or omission came to the Board's attention.<sup>21</sup>

As with inspections, the Board's ability to conduct investigations depends on the Board's ability to obtain documents and information from registered firms and their associated

persons. Pursuant to the Act,<sup>22</sup> the Board has adopted rules under which the Board may (1) require testimony of a registered firm or an associated person thereof with respect to any matter that the Board considers relevant or material to an investigation;<sup>23</sup> (2) require production of audit work papers and any other document or information possessed by a registered firm or associated person, wherever domiciled, that the Board considers relevant or material to an investigation;<sup>24</sup> (3) inspect the books or records of a registered firm or associated person to verify the accuracy of any documents or information supplied;<sup>25</sup> (4) request the testimony of, or any document in the possession of, any other person that the Board considers relevant or material to an investigation, subject to certain limitations;<sup>26</sup> and (5) seek issuance by the Commission, in a manner established by the Commission, of a subpoena requiring the testimony of, or the production of any document in the possession of, any person that the Board considers relevant or material to an investigation.<sup>27</sup>

Pursuant to the Act, a firm's cooperation in and compliance with requests for testimony and for the production of documents made in furtherance of the Board's authority and responsibilities are a condition to the continuing effectiveness of the firm's registration with the Board.<sup>28</sup> Moreover, if a registered firm or associated person refuses to testify, produce documents, or otherwise cooperate with a Board investigation, the Board can impose sanctions, which may include suspending or revoking a firm's registration and suspending or barring an individual from associating with a registered firm.<sup>29</sup> As the Commission has observed, failing to cooperate in a

establish, by rule, a program of inspection with respect to registered firms that provide one or more audit reports for a broker or dealer. See Section 104(a)(2) of the Act. The Board's rules provide for an interim inspection program related to audits of brokers and dealers. See PCAOB Rule 4020T, *Interim Inspection Program Related to Audits of Brokers and Dealers*.

<sup>12</sup> PCAOB Rel. No. 2009-003, at 8-9; see also *Order Approving Proposed Amendment to Board Rules Relating to Inspections*, SEC Exchange Act Release No. 61649, at 5 (Mar. 4, 2010) (observing that inspections are "the cornerstone of the Board's regulatory oversight of audit firms").

<sup>13</sup> See Section 104(a)(1) of the Act. Generally, a registered firm's issuance of an audit report triggers a PCAOB inspection, subject to certain limited exceptions. See Section 104(b)(1) of the Act; PCAOB Rules 4003(a)-(b), *Frequency of Inspections*; see also PCAOB Rules 4003(c) & (e) (identifying certain circumstances in which the Board has discretion to forgo an inspection of a firm). Additionally, the Board conducts inspections of firms that have not issued an audit report with respect to an issuer but have played a substantial role in the preparation or furnishing of such a report. See PCAOB Rule 4003(h).

<sup>14</sup> See Section 104(b)(1) of the Act; see also PCAOB Rules 4003(a)-(b). The Act provides that the Board, by rule, may adjust the annual and triennial inspection schedules if the Board finds that different schedules are consistent with the purposes of the Act, the public interest, and the protection of investors. See Section 104(b)(2) of the Act; see also PCAOB Rules 4003(d)-(g) (adjusting the inspection schedule in certain circumstances).

<sup>15</sup> See Section 104(b)(2) of the Act.

<sup>16</sup> Section 104(d)(1) of the Act.

<sup>17</sup> See Sections 104(d)(2) and 104(d)(3) of the Act.

<sup>18</sup> See Section 102(b)(3) of the Act. Section 102(b)(3)(A) of the Act specifies that each registration application shall contain "a consent executed by the . . . firm to cooperation in and compliance with any request for . . . documents made by the Board in the furtherance of its authority and responsibilities" under the Act. Section 102(b)(3)(B) of the Act, in turn, provides that each registration application shall contain a statement that the firm "understands and agrees that [such] cooperation and compliance . . . shall be a condition to the continuing effectiveness of the registration of the firm with the Board."

<sup>19</sup> See PCAOB Rule 4006; see also *Gately & Assocs., LLC*, SEC Exchange Act Release No. 62656, at 9 (Aug. 5, 2010) ("The obligations under Rule 4006 are unequivocal, and apply to 'any request[] made in furtherance of the Board's authority and responsibilities.'" (quoting Rule 4006)). Documents and information prepared or received by or specifically for the Board in connection with an inspection are confidential and privileged as an evidentiary matter, but the Board may share them with the Commission and, under certain circumstances, with the Attorney General of the United States, certain federal regulators, state attorneys general, certain state regulators, and certain self-regulatory organizations. See Section 105(b)(5)(B) of the Act.

<sup>20</sup> See Section 101(c)(4) of the Act; see also Section 105(a) of the Act.

<sup>21</sup> See Section 105(b)(1) of the Act.

<sup>22</sup> See Section 105(b)(2) of the Act.

<sup>23</sup> See PCAOB Rule 5102, *Testimony of Registered Public Accounting Firms and Associated Persons in Investigations*.

<sup>24</sup> See PCAOB Rule 5103, *Demands for Production of Audit Workpapers and Other Documents from Registered Public Accounting Firms and Associated Persons*.

<sup>25</sup> See PCAOB Rule 5104, *Examination of Books and Records in Aid of Investigations*.

<sup>26</sup> See PCAOB Rule 5105, *Requests for Testimony or Production of Documents from Persons Not Associated with Registered Public Accounting Firms*.

<sup>27</sup> See PCAOB Rule 5111, *Requests for Issuance of Commission Subpoenas in Aid of an Investigation*.

<sup>28</sup> See Section 102(b)(3) of the Act.

<sup>29</sup> See Section 105(b)(3) of the Act; PCAOB Rule 5110, *Noncooperation with an Investigation*.

Board investigation is “very serious misconduct.”<sup>30</sup>

The Act requires the Board to coordinate its investigations with the Commission. The Board must notify the Commission of any pending Board investigation that involves a potential violation of the securities laws, and must thereafter coordinate its work with the Commission’s Division of Enforcement as necessary to protect any ongoing Commission investigation.<sup>31</sup> The Act also authorizes the Board to refer an investigation to the Commission, a self-regulatory organization, certain other federal regulators, and, at the Commission’s direction, certain attorneys general and state regulators.<sup>32</sup>

#### The Board’s Cooperative Framework for International Oversight

The Board has long observed that certain aspects of its inspection and investigation mandates raise special concerns for non-U.S. firms, including potential conflicts with non-U.S. law.<sup>33</sup> Acknowledging these challenges early on, the Board affirmed its commitment “to finding ways to accomplish the goals of the Act without subjecting non-U.S. firms to conflicting requirements.”<sup>34</sup> The Board then worked with its international counterparts where necessary or appropriate, based on norms of international comity, to develop arrangements and working practices to enable the Board and other audit regulators to achieve their respective mandates in a manner responsive to the potential conflicts of law that non-U.S. firms might confront.<sup>35</sup> The Board’s

cooperative approach to oversight of registered firms located outside the United States did not, however, entail any abandonment of the Board’s inspection or investigation mandates or any relinquishment of the Board’s statutory authority to obtain the documents and information it needs from non-U.S. firms in order to execute those mandates.<sup>36</sup>

When the Board adopted its cooperative framework for overseeing non-U.S. registered firms,<sup>37</sup> it rejected calls to afford non-U.S. firms that elected to register with the Board a legal-conflict accommodation during inspections and investigations.<sup>38</sup> In so doing, the Board reiterated that “[p]reserving the Board’s ability to access audit work papers and other documents or information maintained by registered public accounting firms, including non-U.S. registered public accounting firms, is critical to the Board carrying out its obligations under the Act.”<sup>39</sup> For that reason, the Board did not believe that it would be “in the interests of U.S. investors or the public for the Board to adopt a rule of general application that would limit its ability to access such documents or information regardless of the circumstances or need for those documents or information.”<sup>40</sup>

The Commission approved the Board’s rules regarding oversight of non-U.S. firms, which embody the cooperative approach described above.<sup>41</sup> The Commission observed that the PCAOB was discussing potential conflicts of law with foreign audit oversight bodies and encouraged the PCAOB to continue those discussions and to consider ways to work

cooperatively with its international counterparts.<sup>42</sup>

Those discussions have continued, and nearly all have been fruitful. The Board’s oversight programs take into account the possibility that a non-U.S. firm’s obligations under the Act or the Board’s rules might conflict with non-U.S. law. The Board has established procedures that enable non-U.S. firms to assert legal conflicts during the registration and periodic reporting processes so that such firms are not prevented from completing a registration application or complying with periodic reporting requirements.<sup>43</sup> The Board also seeks to coordinate and cooperate with its international counterparts when conducting inspections or investigations in other countries.<sup>44</sup> Nevertheless, in all respects, the Board has made clear that its statutory authority to obtain the documents and information it needs to conduct inspections and investigations has not been relinquished, surrendered, forfeited, or otherwise vitiated.<sup>45</sup>

#### Resolution of Obstacles to Inspections and Investigations in Non-U.S. Jurisdictions

The practices and approaches the Board has successfully developed with foreign regulators to resolve conflicts and to complete inspections and investigations under the Act can differ from jurisdiction to jurisdiction, but they all implement three core principles:

<sup>42</sup> See *id.* at 3.

<sup>43</sup> PCAOB Rule 2105, *Conflicting Non-U.S. Laws*, permits a non-U.S. firm to withhold required information from its registration application based on an asserted conflict with non-U.S. law. That rule allows the Board to treat a registration application as complete if the firm, among other things, submits a copy of the purportedly conflicting non-U.S. law and an accompanying legal opinion. But Rule 2105 does not provide a vehicle for resolving conflicts of law during registration, nor does it apply “to potential conflicts of law that may arise subsequent to registration.” PCAOB Rel. No. 2004–005, at A2–16–A2–18; see also PCAOB Rule 2207, *Assertions of Conflicts with Non-U.S. Laws* (establishing a similar process for registered firms’ annual and special reports to the Board).

<sup>44</sup> See, e.g., Rules on Periodic Reporting by Registered Public Accounting Firms, PCAOB Rel. No. 2008–004, at 32 (June 10, 2008).

<sup>45</sup> See, e.g., *id.* at 41 (“The Board has consistently maintained that, although it will seek to work cooperatively with and through non-U.S. regulators, and although it is willing to accommodate a non-U.S. firm’s reluctance (rooted in an asserted conflict of law) to provide the required written consent to cooperate, each firm ultimately has an obligation to cooperate with the Board to the extent that the Board requires cooperation. The Board does not view this statutory obligation as limited or qualified by non-U.S. legal restrictions.”).

<sup>30</sup> *R.E. Bassie & Co.*, SEC Accounting and Auditing Enforcement Release No. 3354, at 11 (Jan. 10, 2012).

<sup>31</sup> See Section 105(b)(4)(A) of the Act; see also PCAOB Rule 5112(a), *Commission Notification of Order of Formal Investigation*. Documents and information prepared or received by or specifically for the Board in connection with an investigation are confidential and privileged as an evidentiary matter, but the Board may share them with the Commission and, under certain circumstances, with the Attorney General of the United States, certain federal regulators, state attorneys general, certain state regulators, and certain self-regulatory organizations. See Section 105(b)(5)(B) of the Act.

<sup>32</sup> See Section 105(b)(4)(B) of the Act; see also PCAOB Rule 5112(b), Board Referrals of Investigations; PCAOB Rule 5112(c), Commission-directed Referrals of Investigations.

<sup>33</sup> See, e.g., Proposed Rules Relating to the Oversight of Non-U.S. Public Accounting Firms, PCAOB Rel. No. 2003–024, at 3 (Dec. 10, 2003).

<sup>34</sup> *Inspection of Registered Public Accounting Firms*, PCAOB Rel. No. 2003–019, at 5, A2–15–A2–16 (Oct. 7, 2003).

<sup>35</sup> See, e.g., Briefing Paper, *Oversight of Non-U.S. Public Accounting Firms*, PCAOB Rel. No. 2003–020, at 1–2 (Oct. 28, 2003) (“[T]he PCAOB seeks to become partners with its international counterparts in the oversight of the audit firms that operate in

the global capital markets. . . . [A]n arrangement based on mutual cooperation with other high quality regulatory systems respects the cultural and legal differences of the regulatory regimes that exist around the world.”); PCAOB Rel. No. 2003–024, at 8 (“The Board also believes its [cooperative] arrangements may reduce potential conflicts of law . . .”).

<sup>36</sup> PCAOB Rel. No. 2003–020, at 5 (“The Board believes that it is appropriate that a cooperative approach respect the laws of other jurisdictions, to the extent possible. At the same time, every jurisdiction must be able to protect the participants in, and the integrity of, its capital markets as it deems necessary and appropriate.”); accord *Final Rules Relating to Oversight of Non-U.S. Firms*, PCAOB Rel. No. 2004–005, at 3, A2–17 (June 9, 2004).

<sup>37</sup> See generally PCAOB Rel. No. 2004–005.

<sup>38</sup> See *id.* at A2–15–A2–16.

<sup>39</sup> *Id.* at A2–16.

<sup>40</sup> *Id.* at A2–16–A2–17.

<sup>41</sup> See Order Approving Proposed Rules Relating to Oversight of Non-U.S. Registered Public Accounting Firms, SEC Exchange Act Release No. 34–50291, at 3 (Aug. 30, 2004).

(1) The Board must be able to conduct inspections and investigations consistent with its mandate;<sup>46</sup>

(2) The Board must be able to select the audit work and potential violations to be examined;<sup>47</sup> and

(3) The Board must have access to firm personnel, audit work papers, and other information and documents deemed relevant by Board staff.<sup>48</sup>

The Board has been able to accommodate the legal requirements of most non-U.S. jurisdictions without compromising on these three core principles, which the Board considers to be fundamental to its ability to inspect and investigate non-U.S. firms completely.

Building collaborative working relationships with international counterparts based on these principles has taken considerable time and substantial effort, but the Board believes that “it is in the interests of the public and investors for the Board to develop efficient and effective cooperative

arrangements with its non-U.S. counterparts.”<sup>49</sup> The Board now has extensive experience with cooperative arrangements that successfully resolve conflicts and allow the PCAOB and its international counterparts to satisfy their respective oversight mandates.

#### Board Inspections of Non-U.S. Firms

Inspections of non-U.S. firms began in 2005,<sup>50</sup> and the Board quickly identified obstacles that required negotiation with its international counterparts. When a registered firm issuing audit reports for an issuer is located in a non-U.S. jurisdiction that has an auditor oversight authority of its own, the Board seeks to engage with that local regulator. The PCAOB conducts many inspections of non-U.S. firms jointly with local authorities, using approaches that take into consideration the laws and practices of the local jurisdiction. The Board also developed a specific regulatory framework for assessing the degree, if any, to which the Board may rely on the inspection work of the local regulator in an effort to reduce redundancy.<sup>51</sup> Even where the Board conducts its own inspection rather than a joint inspection with a local auditor oversight authority, the Board may communicate with its international counterpart regarding the Board’s inspections in the jurisdiction.<sup>52</sup>

By December 2008, the Board had inspected non-U.S. firms in 24 jurisdictions.<sup>53</sup> But the Board also observed that home-country legal obstacles and sovereignty concerns were impeding the Board’s ability to conduct inspections of some non-U.S. firms.<sup>54</sup> Given these obstacles, the Board, in 2009, adjusted the schedule for its first inspections of non-U.S. firms in certain

jurisdictions so that the Board could continue its efforts to reach cooperative arrangements with those firms’ home-country regulators.<sup>55</sup>

In so doing, however, the Board expressly rejected the suggestion that it should exempt from inspection non-U.S. firms “that cannot cooperate with PCAOB inspections due to legal conflicts or sovereignty-based opposition from their local governments,” finding that exempting such firms from inspections is not in the interests of investors or the public.<sup>56</sup> Instead, the Board reaffirmed the ultimate obligation of all registered firms, including non-U.S. firms, to be subject to inspection and to comply with the Board’s inspection-related requests.<sup>57</sup>

The Commission, in approving the Board’s extension of the deadline for the first inspections of certain non-U.S. firms, recognized that “the adjustment would provide additional time [for the Board] to continue discussions on outstanding matters and work towards cooperation and coordination with authorities in all relevant jurisdictions.”<sup>58</sup> And in connection with its approval of other adjustments to the inspection schedule of non-U.S. firms, the Commission stated that “the PCAOB should continue to work toward cooperative arrangements with the appropriate local auditor oversight authorities where it is reasonably likely that appropriate cooperative arrangements can be obtained.”<sup>59</sup>

By the end of 2009, the Board had conducted inspections of non-U.S. firms in an additional nine jurisdictions, bringing the cumulative total to 33 jurisdictions.<sup>60</sup> The Board, however,

<sup>46</sup> See, e.g., Section 104(a)(1) of the Act (requiring a “continuing program of inspections”); Section 104(b)(1) of the Act (establishing inspection frequency requirements); Section 104(c) of the Act (requiring identification of non-compliant acts, practices, or omissions to act, and providing for reporting of such conduct to the Commission and appropriate state regulatory authorities, when appropriate); Section 105(b)(1) of the Act (authorizing Board investigations); Section 105(b)(3) of the Act (authorizing the imposition of sanctions for noncooperation with an investigation); Section 105(b)(4) of the Act (requiring coordination with the Commission’s Division of Enforcement and authorizing referrals of investigations in certain circumstances); Section 105(b)(5)(B)(i) of the Act (authorizing the Board to share with the Commission documents received in connection with an inspection or investigation).

<sup>47</sup> See, e.g., Section 104(d)(1) of the Act (directing the Board to inspect and review audit and review engagements “as selected by the Board”); Section 104(d)(3) of the Act (authorizing the Board to perform other testing of audit, supervisory, and quality control procedures as are necessary or appropriate in light of the purpose of the inspection and the responsibilities of the Board); Section 105(b)(1) of the Act (authorizing the Board to conduct an investigation of “any” act, practice, or omission to act by a registered firm or an associated person thereof that may violate “any” provision of the Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission under the Act, or professional standards).

<sup>48</sup> See, e.g., Section 104(d)(1) of the Act (directing the Board to inspect and review audit and review engagements); Section 104(d)(2) of the Act (directing the Board to evaluate the sufficiency of a registered firm’s quality control system, including the manner of the documentation and communication of that system); Section 105(b)(2)(A)–(B) of the Act (authorizing the Board to require the testimony of, and the production of audit work papers and any other documents or information from, registered firms and their associated persons, wherever domiciled, and to inspect the books and records of such firm or associated person to verify the accuracy of any documents or information supplied).

<sup>49</sup> PCAOB Rel. No. 2009–003, at 4–5.

<sup>50</sup> See *Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms*, PCAOB Rel. No. 2008–007, at 4 (Dec. 4, 2008).

<sup>51</sup> See PCAOB Rel. No. 2009–003, at 5–6. Non-U.S. firms may formally request that the Board rely on a non-U.S. inspection to the extent deemed appropriate by the Board, and the Board will examine certain factors to determine the degree, if any, to which the Board may rely on the non-U.S. inspection. See PCAOB Rule 4011, *Statement by Foreign Registered Public Accounting Firms*; PCAOB Rule 4012, *Inspections of Foreign Registered Public Accounting Firms*; PCAOB Rel. No. 2009–003, at 5. In contrast to an exemption, reliance on a non-U.S. inspection pursuant to Rule 4012 is a cooperative approach that can be used when efficient and appropriate.

<sup>52</sup> See PCAOB Rel. No. 2009–003, at 5.

<sup>53</sup> See PCAOB Rel. No. 2008–007, at 4 & n.9 (inspections had been conducted in Argentina, Australia, Bermuda, Brazil, Canada, Chile, Colombia, Greece, Hong Kong, India, Indonesia, Ireland, Israel, Japan, Kazakhstan, Mexico, New Zealand, Panama, Peru, Singapore, South Africa, South Korea, Taiwan, and the United Kingdom).

<sup>54</sup> PCAOB Rel. No. 2009–003, at 5.

<sup>55</sup> See *id.* at 9.

<sup>56</sup> See *id.* at 8–9.

<sup>57</sup> See *id.* at 13–14 (“[F]irms must register with the Board in order to engage in certain professional activity directly related to, and affecting, U.S. financial markets, and all registered firms are subject to the Act and the rules of the Board irrespective of their location. A registered firm is subject to various requirements and conditions, including PCAOB Rule 4006’s requirement to cooperate in an inspection. In addition, as reflected in Section 102(b)(3) of the Act, a firm’s compliance with Board requests for information is a condition of the continuing effectiveness of the firm’s registration with the Board.”). The Board also reiterated that it “does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding . . . for failing or refusing to provide information requested in an inspection.” *Id.* at 14; accord PCAOB Rel. No. 2008–007, at 16 n.35.

<sup>58</sup> Order Approving Proposed Amendment to Board Rules Relating to Inspections, SEC Exchange Act Release No. 34–59991, at 3 (May 28, 2009).

<sup>59</sup> *Id.* at 5.

<sup>60</sup> See *Jurisdictions in Which the PCAOB Has Conducted Inspections (as of Dec. 31, 2009)* (Feb.

was still prevented from inspecting registered firms in mainland China, Hong Kong (to the extent an audit encompassed a company's operations in mainland China), Switzerland, and the European countries required to follow the European Union's Directive on Statutory Auditors.<sup>61</sup>

The Board responded to these obstacles in several ways<sup>62</sup> and, since 2010, the Board has inspected non-U.S. firms in an additional 20 jurisdictions, bringing the total number of non-U.S. jurisdictions in which the PCAOB has conducted inspections to 53.<sup>63</sup> Where

3, 2010), available at [https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/inspections/documents/12-31-jurisdictions.pdf?sfvrsn=2c09bd73\\_0](https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/inspections/documents/12-31-jurisdictions.pdf?sfvrsn=2c09bd73_0) (adding Belize, Bolivia, Cayman Islands, Norway, Papua New Guinea, Philippines, Russia, Ukraine, and United Arab Emirates).

<sup>61</sup> See PCAOB Publishes Updated Staff Guidance Related to Registration Process for Applicants from Certain Non-U.S. Jurisdictions (June 1, 2010), available at <https://org/events/news-releases/news-release-detail/pcaob-publishes-updated-staff-guidance-related-to-registration-process-for-applicants-from-certain-non-u-s-jurisdictions> 289.

<sup>62</sup> In 2009, the Board began publishing a list of registered firms whose first inspections were overdue, which identified the jurisdiction in which each firm was located. See PCAOB Rel. No. 2009-003, at 10-11. In 2010, the Board expanded the publication to include a list of non-U.S. public companies with securities traded in U.S. markets that had retained a registered firm the Board could not inspect because of asserted restrictions based on non-U.S. law or objections on grounds of national sovereignty (the "Denied Access List"). See PCAOB Publishes List of Issuer Audit Clients of Non-U.S. Registered Firms in Jurisdictions where the PCAOB is Denied Access To Conduct Inspections (May 18, 2010), available at <https://pcaobus.org/news-events/news-releases/news-release-detail/pcaob-publishes-list-of-issuer-audit-clients-of-non-u-s-registered-firms-in-jurisdictions-where-the-pcaob-is-denied-access-to-conduct-inspections> 284 ("The auditors of the issuers appearing on this list are located in [mainland] China, Hong Kong, Switzerland, and 18 European Union countries. The PCAOB continues to work to eliminate obstacles to inspections in these jurisdictions.").

Also, in October 2010, the Board modified its approach to registration applications from firms in jurisdictions where there were unresolved obstacles to inspections, stating that "its consideration of new applications from firms in those jurisdictions will no longer be premised on an expectation that those obstacles will be resolved without undue delay to any necessary PCAOB inspection of the firm." *Consideration of Registration Applications From Public Accounting Firms in Non-U.S. Jurisdictions Where There Are Unresolved Obstacles to PCAOB Inspections*, PCAOB Rel. No. 2010-007, at 2-3 (Oct. 7, 2010). A list of those jurisdictions is maintained on the PCAOB's website. See Frequently Asked Questions Regarding Issues Relating to Non-U.S. Accounting Firms (Apr. 20, 2021), available at [https://pcaobus.org/oversight/registration/non\\_us\\_registration\\_faq](https://pcaobus.org/oversight/registration/non_us_registration_faq) (FAQ 6).

<sup>63</sup> See *Non-U.S. Jurisdictions Where the PCAOB has Conducted Oversight*, available at <https://pcaobus.org/oversight/international/international/pcaob-inspections-of-registered-non-u-s-firms> (adding Austria, Bahamas, Denmark, Finland, France, Germany, Hungary, Italy, Jamaica, Luxembourg, Malaysia, Netherlands, Nicaragua, Nigeria, Pakistan, Spain, Sweden, Switzerland, Thailand, and Turkey).

needed, the Board enters into formal bilateral cooperative agreements with non-U.S. regulators, and has done so with authorities in 25 jurisdictions.<sup>64</sup> The Board continues to publish its Denied Access List, which identifies the jurisdictions where the PCAOB cannot conduct inspections because foreign authorities have denied access, the auditors from those jurisdictions that issued audit reports filed with the Commission, and those auditors' non-U.S. public company clients.<sup>65</sup> The Board also still adheres to the registration approach it adopted in 2010 and maintains a public list of the jurisdictions whose applicants are subject to that approach.<sup>66</sup>

All told, more than 840 non-U.S. firms from more than 80 jurisdictions are registered with the Board. Over 200 of those firms, from more than 40 jurisdictions, are presently subject to PCAOB inspection on a triennial basis because they have chosen to audit issuers.<sup>67</sup> As of the date of this release, as reflected on the Board's website,<sup>68</sup> the Board can conduct inspections everywhere it needs to do so except in mainland China and Hong Kong.

#### Board Investigations of Non-U.S. Firms

The Board has conducted numerous investigations in which it appeared that an act, practice, or omission to act by a

<sup>64</sup> See PCAOB Cooperative Arrangements with Non-U.S. Regulators, available at <https://pcaobus.org/international/regulatorycooperation>. Although a formal bilateral agreement is not necessarily a prerequisite to a PCAOB inspection in a non-U.S. jurisdiction, the PCAOB often enters into such agreements with foreign audit regulators to minimize administrative burdens and potential legal or other conflicts that non-U.S. firms might face in their home countries.

<sup>65</sup> See Audit Reports Issued by PCAOB-Registered Firms in Jurisdictions where Authorities Deny Access to Conduct Inspections, available at <https://pcaobus.org/oversight/international/denied-access-to-inspections> (identifying jurisdictions where the Board has been denied access to conduct inspections).

<sup>66</sup> See Frequently Asked Questions Regarding Issues Relating to Non-U.S. Accounting Firms (Apr. 20, 2021), available at [https://pcaobus.org/oversight/registration/non\\_us\\_registration\\_faq](https://pcaobus.org/oversight/registration/non_us_registration_faq) (FAQ 6, identifying jurisdictions where obstacles to inspection exist). This list of jurisdictions is broader than the Denied Access List, because this list includes certain European jurisdictions where the Board presently does not need to conduct inspections because no registered firms in the jurisdiction are issuing audit reports, but where an agreement regarding inspections would need to be reached before any future inspections could take place.

<sup>67</sup> Currently, there are no non-U.S. firms that the PCAOB is required by the Act to inspect on an annual basis.

<sup>68</sup> See International, available at <https://pcaobus.org/oversight/international> (providing a map showing where the Board currently is able to conduct oversight of registered firms and where the Board currently is denied the necessary access to conduct oversight activities).

non-U.S. firm or its associated persons might have violated an applicable law, rule, or standard. In the course of those investigations, the Board has used a variety of tools, provided for in the Act and the Board's rules, to access relevant documents and information. Using those tools, the Board has requested and obtained audit work papers and other documents and information from non-U.S. firms and associated persons, and has conducted interviews and testimony of non-U.S. firm personnel.

In many of those instances, the Board coordinated its investigation with a non-U.S. regulator with which it had entered a bilateral cooperative arrangement. Those cooperative arrangements have allowed the Board and its international counterpart to communicate and share information, facilitating the Board's access to the documents and information it needed to conduct the investigation. In some but not all circumstances, in parallel with the Board's investigation, a non-U.S. regulator may conduct its own investigation of the same firm or associated persons for possible violations under the regulator's laws and standards.

Many of the Board's investigations of non-U.S. firms or their associated persons remain confidential, because Board investigations are non-public and cannot be disclosed unless they have resulted in the imposition of disciplinary sanctions.<sup>69</sup> The Board does, however, disclose its settled and adjudicated disciplinary orders imposing sanctions.<sup>70</sup> To date, the Board has sanctioned more than 50 non-U.S. registered firms and more than 60 associated persons of such firms, from 24 non-U.S. jurisdictions.<sup>71</sup> In addition to the investigations that resulted in the imposition of sanctions, the Board also has conducted investigations that did not result in sanctions in numerous other non-U.S. jurisdictions. Yet despite these results, the Board has been unable to complete some investigations of non-U.S. firms or their personnel because they refused to cooperate with an investigation based on a position taken

<sup>69</sup> See Section 105(b)(5)(A) of the Act.

<sup>70</sup> When the Board imposes sanctions, the Board's disciplinary action is stayed if the respondent applies for Commission review of the Board's order or if the Commission initiates such review on its own. In either situation, the Board's sanctions remain stayed (and non-public) unless and until the Commission lifts the stay. See Section 105(e)(1) of the Act. After the stay is lifted, the Board's order may be made public. See Section 105(d)(1)(C) of the Act.

<sup>71</sup> See Enforcement Actions, available at <https://pcaobus.org/oversight/enforcement/enforcement-actions>.

by non-U.S. authorities in their jurisdiction.<sup>72</sup>

#### The Holding Foreign Companies Accountable Act

Against this backdrop, Congress enacted the HFCAA. The HFCAA, which amends Section 104 of the Act, calls for the Board to determine whether it is unable to inspect or investigate completely registered firms located in a foreign jurisdiction because of a position taken by an authority in that jurisdiction.<sup>73</sup> The HFCAA, among other things, also mandates that after the Board makes such a determination, the Commission shall require covered issuers that retain firms subject to the Board's determination to make certain disclosures in their annual reports and, eventually, if certain conditions persist, shall prohibit trading in those issuers' securities.<sup>74</sup>

The Board's determinations under the HFCAA supplement, rather than supplant, the Board's other authorities under the Act. A registered firm's cooperation in and compliance with Board requests during inspections and investigations continues to be a condition to the continuing effectiveness of its registration with the Board. Failure to cooperate with a Board inspection or investigation still can result in the imposition of disciplinary sanctions, including civil money penalties and revocation of the firm's registration. Therefore, firms must consider their obligations to comply with PCAOB inspection and investigation demands when they choose to become and remain registered with the Board and when they accept or continue client engagements.

#### Discussion of the Proposed Rule

The HFCAA does not specify the procedure the Board should follow when making determinations. Nor does the HFCAA specify the content of the Board's determinations; the manner in which any such determination should

be shared with the Commission; how, and in what format, any such determination should be made publicly available; the effective date or duration of any such determination; or the manner in which any such determination can be reaffirmed, modified, or vacated. The proposed rule establishes those facets of the Board's determination process.

Although the HFCAA does not expressly require the Board to adopt a rule governing the determinations it makes under the statute, the Board believes that a rule will inform investors, registered firms, issuers, audit committees, foreign authorities, and the public at large as to how the Board will perform its functions under the statute. Furthermore, a Board rule will promote consistency in the Board's processes regarding determinations under the HFCAA.<sup>75</sup> Commenters generally agreed that a rule governing the Board's determination process would promote transparency and consistency and reduce regulatory uncertainty.

#### Two Types of Board Determinations Under the HFCAA

The HFCAA requires that the Board determine whether it is unable to inspect or investigate completely registered public accounting firms that have a branch or office that is located in a foreign jurisdiction because of a position taken by one or more authorities in that jurisdiction. The proposed rule provides that the Board may make two types of determinations: Determinations as to a particular foreign jurisdiction and determinations as to a particular registered firm. Those two types of determinations are addressed in subparagraphs (a)(1) and (a)(2) of proposed Rule 6100.

#### Determinations as to Registered Firms Headquartered in a Particular Foreign Jurisdiction

The Board believes that firms headquartered in a foreign jurisdiction necessarily have a branch or office that is located in that jurisdiction. Taking that into account, subparagraph (a)(1) of the proposed rule provides that the Board may determine that it is unable to inspect or investigate completely registered firms<sup>76</sup> headquartered in a

foreign jurisdiction because of a position taken by one or more authorities in that jurisdiction. In other words, a jurisdiction-wide determination under subparagraph (a)(1) would apply to all firms *headquartered* in that jurisdiction.

The Board adopted subparagraph (a)(1) as proposed. Commenters generally supported the Board's proposed approach to jurisdiction-wide determinations. Several commenters noted that jurisdiction-wide determinations would be consistent with the HFCAA or otherwise appropriate, and several other commenters stated that having such determinations apply to firms that are headquartered in the jurisdiction would likewise be appropriate. No commenter asserted that jurisdiction-wide determinations would be inconsistent with the HFCAA or otherwise inappropriate.

The Board believes that a jurisdiction-wide approach to its determinations under the HFCAA is consistent with the structure of the statute. The statute requires the Board's determinations to be based on "a position taken by an authority in the foreign jurisdiction." It follows that if a foreign authority articulates or maintains a position that applies generally to PCAOB inspections or investigations in a foreign jurisdiction, that position could provide the basis for a jurisdiction-wide determination. Hence, the statute, in the Board's view, can reasonably be interpreted to allow the Board to make jurisdiction-wide determinations.<sup>77</sup>

Having a jurisdiction-wide approach at the Board's disposal is important for consistency and efficiency. When the obstacles to completing inspections and investigations are not specific to individual registered firms, but instead reflect threshold or general positions taken by a foreign authority, the Board believes that it should be able to address those obstacles on a jurisdiction-wide basis in a consistent manner and in a single determination. Under those circumstances, separate determinations as to each registered firm in the jurisdiction should not be required.

The proposed rule provides that jurisdiction-wide determinations would be limited to registered firms that are

inspects registered firms and investigates potential violations by registered firms or their associated persons. Accordingly, the proposed rule refers to the Board's inability to inspect or investigate registered firms.

<sup>77</sup> See, e.g., 166 Cong. Rec. H6033 (daily ed. Dec. 2, 2020) (statement of Rep. Gonzalez) ("[T]he act should be read to apply to companies where the auditor that signs the audit report is located in a jurisdiction that does not permit PCAOB inspection access.").

<sup>72</sup> See, e.g., *Crowe Horwath (HK) CPA Limited*, PCAOB Rel. No. 105–2017–031 (July 25, 2017) (noncooperation with a Board investigation based on positions taken by Chinese authorities); *Kim Wilfred Ti*, PCAOB Rel. No. 105–2016–004 (Jan. 12, 2016) (same); *Derek Wan Tak Shing*, PCAOB Rel. No. 105–2016–003 (Jan. 12, 2016) (same); *Edith Lam Kar Bo*, PCAOB Rel. No. 105–2016–002 (Jan. 12, 2016) (same); *PKF (Hong Kong)*, PCAOB Rel. No. 105–2016–001 (Jan. 12, 2016) (same).

<sup>73</sup> See HFCAA § 2(i)(2)(A), 15 U.S.C. 7214(i)(2)(A) (requiring that the Commission identify certain issuers that "retain[] a registered public accounting firm that has a branch or office that . . . is located in a foreign jurisdiction . . . and . . . the Board is unable to inspect or investigate completely because of a position taken by an authority in [that] foreign jurisdiction . . . , as determined by the Board").

<sup>74</sup> See HFCAA §§ 2(i)(2)(B), 2(i)(3), 3(b), 15 U.S.C. 7214(i)(2)(B), 7214(i)(3), 7214a(b).

<sup>75</sup> The Act states that "[t]he rules of the Board shall, subject to the approval of the Commission[,] . . . provide for the operation and administration of the Board, the exercise of its authority, and the performance of its responsibilities under this Act." Section 101(g)(1) of the Act.

<sup>76</sup> The HFCAA refers to a firm's "branch or office" that the Board is unable to inspect or investigate completely. HFCAA § 2(i)(2)(A)(i), 15 U.S.C. 7214(i)(2)(A)(i). The Board does not inspect or investigate branches or offices. Rather, the Board



“headquartered” in the jurisdiction. The Board believes that a position taken by a foreign authority will impact registered firms headquartered in the jurisdiction, but its impact on firms that are headquartered elsewhere can turn on multiple factors, including the extent of a firm’s presence in the jurisdiction and the nature and extent of the audit work it performs in that jurisdiction. Limiting jurisdiction-wide determinations to firms that are headquartered in the jurisdiction is intended to ensure that these determinations are appropriately tailored and do not encompass firms that have a physical presence of any kind, or personnel of any number, in the jurisdiction. Consistent with the scope of the HFCAA, however, the proposed rule provides that the Board may make individualized determinations as to firms that have an “office” in a noncooperative jurisdiction but are headquartered elsewhere, as discussed below.

A firm is “headquartered,” as that term is used in the proposed rule, at its principal place of business (*i.e.*, where the firm’s management directs, controls, and coordinates the firm’s activities).<sup>78</sup> The Board would presume that a firm is headquartered at the physical address reported by the firm as its headquarters to the Board in the firm’s required filings.<sup>79</sup> Absent an indication that the headquarters address reported by a firm may not be its principal place of business, the Board would use that address to determine where the firm is “headquartered” for purposes of the proposed rule. If questions arise as to whether a firm’s reported headquarters address is the firm’s principal place of business, however, the Board may consider other relevant and reliable information regarding the firm and may request additional information from the firm pursuant to the Board’s rules when determining where a firm is headquartered.<sup>80</sup>

<sup>78</sup> See, e.g., *Hertz Corp. v. Friend*, 559 U.S. 77, 92–93 (2010) (defining “principal place of business” in the context of federal diversity jurisdiction, and further explaining that “in practice it should normally be the place where the corporation maintains its headquarters—provided that the headquarters is the actual center of direction, control, and coordination, *i.e.*, the ‘nerve center,’ and not simply an office where the corporation holds its board meetings”).

<sup>79</sup> When registering with the Board, an applicant must provide its “HEADQUARTERS PHYSICAL ADDRESS” in Item 1.2.1 of its application for registration on Form 1. Each year thereafter, in Item 1.2.a of its annual report on Form 2, a firm must provide the “Physical address of the Firm’s headquarters office.”

<sup>80</sup> See PCAOB Rule 4000(b) (“In furtherance of the Board’s inspection process, the Board may at any time request that a registered public accounting

Several commenters stated that it was appropriate for the Board to look at a firm’s required filings with the Board in the first instance for information as to where the firm is headquartered. One commenter suggested that the Board look beyond such filings and also consider a firm’s filings with its home-country regulator as well as other facts and circumstances regarding the firm. As noted in the preceding paragraph, the Board retains the ability to request and consider additional information—including the information identified by the commenter—if any questions arise regarding the location of a firm’s headquarters. Another commenter, contemplating that the Board might look to filings of Form AP for information as to where a firm is headquartered, cautioned that such forms may not be timely filed.<sup>81</sup> The Board intends to rely on annual reports on Form 2 rather than Form APs for such information, though the Board is not precluded from considering information on Form APs or any other relevant and reliable information.<sup>82</sup>

In some instances, a member firm of an international firm network might be headquartered in a jurisdiction that becomes subject to a jurisdiction-wide determination of the Board. In such a circumstance, if that member firm is a separate legal entity from the other member firms in the network and signs audit reports in its own name, the Board would not treat other member firms in the network as being “located” or having an “office” in that jurisdiction merely because they are part of the same network as a member firm subject to the jurisdiction-wide determination.<sup>83</sup> One

firm provide to the Board additional information or documents relating to information provided by the firm in any report filed pursuant to Section 2 of these Rules, or relating to information that has otherwise come to the Board’s attention.”). This approach aligns with the Board’s decade-long practice when assessing registration applications from firms located in non-U.S. jurisdictions where there are obstacles to PCAOB inspections. This approach has been applied to applicants that are headquartered in such jurisdictions, and the Board has sought additional information from applicants when necessary to assess where they are headquartered.

<sup>81</sup> Item 3.1.7 of Form AP identifies the office (not the headquarters) of the firm that issued the audit report for the referenced audit engagement, but Item 4.1 of Form AP identifies the headquarters’ office location of the other accounting firms that contributed 5% or more of the total audit hours.

<sup>82</sup> In any event, PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants*, already requires timely filing of accurate Form APs, and the failure to comply with that rule can provide the basis for inspection findings or disciplinary sanctions.

<sup>83</sup> See SEC Exchange Act Release No. 91364, at 4 n.8.

commenter addressed this topic and agreed with this approach.

Based on its experience with inspections and investigations in foreign jurisdictions, the Board anticipates that most determinations made under proposed Rule 6100 would be jurisdiction-wide determinations under subparagraph (a)(1). Historically, the positions taken by foreign authorities have impaired the Board’s ability to conduct inspections or investigations in the jurisdiction generally.

Some of the positions taken by foreign authorities have been based upon “gatekeeper” laws, which provide that a registered firm can transfer its audit work papers to the Board only via a local non-U.S. regulator. (By contrast, no audit oversight law in the U.S. requires foreign auditor oversight authorities to involve the PCAOB when seeking audit work papers from a U.S. firm.) As noted above, the Board has considerable experience resolving conflicts that arise from gatekeeper laws using bilateral arrangements, or statements of protocol, whereby the non-U.S. regulator facilitates the PCAOB’s access to audit work papers and associated information that registered firms are obligated to provide to the Board upon request. The Board’s ability to conduct inspections or investigations could become impaired in any of these jurisdictions, however, if such an arrangement were terminated; if non-performance under an arrangement were significant; or if, in the case of countries within the European Economic Area, an arrangement were rendered ineffective because the European Commission revoked or failed to renew its “adequacy decision” regarding the PCAOB.<sup>84</sup> The resulting impairment would have jurisdiction-wide impact, and thus could give rise to a jurisdiction-wide determination under subparagraph (a)(1) of the proposed rule. The Board believes that a jurisdiction-wide determination would be an efficient, appropriate response to such an impairment.

<sup>84</sup> Article 47 of the Directive 2014/56/EU of the European Parliament and of the Council of 16 April 2014 amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts requires that the European Commission issue an adequacy decision regarding a third country audit regulator (such as the PCAOB) and that regulator’s ability to safeguard audit work papers and related confidential information before a European Union member state audit regulator can execute a working arrangement allowing firms to provide access to such information. See Directive 2014/56/EU, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32014L0056>. The European Commission’s July 2016 adequacy decision with respect to the PCAOB is set to expire in July 2022.



Apart from gatekeeper laws, foreign authorities' positions also may be based on other substantive laws (e.g., personal data protection laws, state secrecy laws, banking secrecy laws, or commercial secrecy laws) that impair the Board's ability to conduct inspections or investigations by obstructing the Board's access to firm personnel, audit work papers, or other documents or information relevant to an inspection or investigation. The Board also has considerable experience working collaboratively with non-U.S. regulators to employ working practices that enable compliance with such non-U.S. laws without impairing the Board's ability to complete inspections or investigations. The proposed rule contemplates circumstances in which a cooperative resolution to those legal conflicts might not be achieved.

In those circumstances, the Board believes that investors and the public interest would be best served by making a jurisdiction-wide determination under the HFCAA, even if the foreign jurisdiction's law (or interpretation or application of that law) affects the Board's ability to inspect or investigate only certain types of audit engagements. For instance, a foreign jurisdiction might deny to the PCAOB access to critical parts of the audit work papers for entities operating in a particular business sector (e.g., financial services) or with particular business models (e.g., state-owned enterprises). In such a case, even if only a few registered firms in that jurisdiction presently are auditing issuers in that sector or with that business model, the Board would assess whether its access would be equally impaired should any registered firm in the jurisdiction perform the restricted engagements. If the foreign authority's position applies generally to firms within the jurisdiction, then it impairs the Board's ability to conduct inspections or investigations completely on a jurisdiction-wide basis, regardless of the differences among registered firms' client portfolios at the time of the Board's determination. No commenter challenged this reasoning, nor did any commenter suggest that investors or the public interest would be better served if the Board were to make determinations as to particular firms, rather than jurisdiction-wide determinations, in such circumstances.

In the situation described above, the Board does not believe that firm-by-firm determinations would be appropriate. While the Board could make a determination as to particular firms under subparagraph (a)(2) of the proposed rule based, for instance, on the composition of each firm's client

portfolio at a moment in time, the Board believes that such an approach may not effectively accomplish the HFCAA's objectives. For instance, it might incentivize an issuer whose audit engagement cannot be inspected or investigated by the Board (a financial institution or state-owned enterprise in the example) to switch audit firms frequently. Specifically, if the issuer's audit firm were made subject to a Board determination under the HFCAA, the issuer could switch to another audit firm in the jurisdiction that had not previously handled a restricted engagement and, when the Board subsequently issued a determination under the HFCAA as to the issuer's new audit firm, the issuer could switch yet again. Such purposeful migration by issuers could trigger a perpetual cycle of Board determinations as to particular audit firms, while the issuers potentially evade some or all of the intended consequences of the HFCAA. A jurisdiction-wide determination, by contrast, would eliminate these concerns. No commenter disagreed with this analysis or the Board's rationale.

The jurisdiction-wide determinations contemplated by subparagraph (a)(1) of the proposed rule also comport with the historical practice of identifying publicly the jurisdictions where there are unresolved obstacles to Board inspections or investigations. Since 2010, information of this kind has been posted on the PCAOB's website, for two purposes: To notify investors and potential investors of the public companies whose audit reports were issued by firms from those jurisdictions, and to notify firms considering potential registration with the Board of the consequences of obstacles to inspections in their jurisdictions.<sup>85</sup>

Jurisdiction-wide determinations would rest, as the HFCAA directs, on whether the Board is able "to inspect or investigate completely" firms in the jurisdiction. The HFCAA, however, does not define what it means "to inspect or investigate completely." The Board does not view that phrase as limited to instances where the Board started, but was unable to finish, an inspection or investigation of a

registered firm, because foreign authorities' positions also can make it impossible or infeasible, as a practical matter, for the Board to attempt to commence such inspections or investigations in the first place. In other words, the Board may make a determination under the HFCAA under a range of circumstances, including when it is not able to commence an inspection or investigation or when, based on the Board's knowledge and experience, it has concluded that commencing an inspection or investigation would be futile as a result of the position taken by a foreign authority.

With that in mind, the proposed rule ties the Board's ability to "inspect or investigate completely" to the three core principles that guide the Board's framework for international cooperation. Specifically, the Board will consider whether it (1) can select the audits and audit areas it will review during inspections and the potential violations it will investigate; (2) has timely access to firm personnel, audit work papers, and other documents and information relevant to its inspections and investigations, and the ability to retain and use such documents and information; and (3) can otherwise conduct its inspections and investigations in a manner consistent with the Act and the Board's rules. For a further discussion of how these three principles would inform the Board's assessment of whether it can "inspect or investigate completely," see below.

The Board's jurisdiction-wide determinations under the proposed rule would be based on "a position taken by one or more authorities" in the foreign jurisdiction. While the proposed rule refers to a singular "position," that term encompasses all of the various positions taken by authorities in the jurisdiction that, when aggregated together, collectively constitute the position of authorities in the jurisdiction. In a similar vein, the proposed rule's reference to "one or more authorities" acknowledges that, in some jurisdictions, multiple authorities can take positions that impair the Board's ability to conduct inspections or investigations. Those "authorities" are not limited to a "foreign auditor oversight authority," as that phrase is defined in the Act,<sup>86</sup> but rather include any authority whose position can obstruct the Board's oversight. Such authorities may include, for example, securities regulators, industry regulators, data protection authorities, national security bodies, foreign

<sup>85</sup> See Audit Reports Issued by PCAOB-Registered Firms in Jurisdictions where Authorities Deny Access to Conduct Inspections, available at <https://pcaobus.org/oversight/international/denied-access-to-inspections>; Frequently Asked Questions Regarding Issues Relating to Non-U.S. Accounting Firms (Apr. 20, 2021), available at [https://pcaobus.org/oversight/registration/non\\_us\\_registration\\_faq](https://pcaobus.org/oversight/registration/non_us_registration_faq) (FAQ 6); see also International, available at <https://pcaobus.org/oversight/international/> (providing map showing where the Board currently can and cannot conduct oversight activities).

<sup>86</sup> See Section 2(a)(17) of the Act.

ministries, or authorities of political subdivisions (*e.g.*, a provincial authority).

#### Determinations as to a Particular Registered Firm With an Office in a Foreign Jurisdiction

Although the Board anticipates that most determinations under the proposed rule would be jurisdiction-wide determinations, the Board cannot anticipate every scenario that it might encounter when conducting oversight of firms in foreign jurisdictions. In light of that practical limitation, subparagraph (a)(2) of the proposed rule provides that the Board may determine that it is unable to inspect or investigate completely a particular registered firm that has an office<sup>87</sup> located in a foreign jurisdiction because of a position taken by one or more authorities in that jurisdiction. This provision would complement the Board's ability to make jurisdiction-wide determinations in two important respects.

First, if a foreign authority obstructs a Board inspection or investigation of a particular firm headquartered in the jurisdiction—but does not obstruct inspections or investigations in a more general manner that might apply to all firms in the jurisdiction—subparagraph (a)(2) provides the Board with an avenue for making a more tailored determination under the HFCAA when a jurisdiction-wide determination might be inappropriately broad.

Second, subparagraph (a)(2) allows the Board to make determinations under the HFCAA as to firms that are not headquartered in the foreign authority's jurisdiction but have an office located there. In this respect, a determination under subparagraph (a)(2) can supplement a jurisdiction-wide determination under subparagraph (a)(1) that applies to firms headquartered in the jurisdiction. Furthermore, the reach of subparagraph (a)(2) ensures that the Board's determinations under the proposed rule can match the scope of its mandate under the HFCAA.

The Board's approach to determining where a firm's offices are located is similar to the Board's approach to

determining where a firm is headquartered. The Board will look principally to the firm's filings with the Board,<sup>88</sup> but if there is any uncertainty as to whether a firm has an office in a jurisdiction, the Board may consider other information regarding the firm and may request additional information from the firm pursuant to Rule 4000(b).

Apart from those two distinguishing features (namely, that determinations are directed to a particular firm and can reach firms that have an office in the foreign jurisdiction but are not headquartered there), subparagraph (a)(2) mirrors the operation of subparagraph (a)(1). The Board's inability "to inspect or investigate completely" is tied to the three principles that guide the Board's approach to international cooperation, as noted above and discussed further below. The phrase "position taken by one or more authorities" has the same meaning as in subparagraph (a)(1). Finally, if a member firm of an international firm network becomes subject to a Board determination under subparagraph (a)(2), and is a separate legal entity from the other member firms in the network and signs audit reports in its own name, the Board would not treat it as an "office" of other member firms within the network, and accordingly the other member firms would not be subject to that Board determination under subparagraph (a)(2).

The Board adopted subparagraph (a)(2) as proposed, except for one addition to the subparagraph's title.<sup>89</sup> Commenters generally supported the Board's proposed approach to determinations as to a particular registered firm and stated that the distinction between those determinations and the jurisdiction-wide determinations contemplated in subparagraph (a)(1) is clear. Several commenters also stated that it is appropriate for the Board to look at a firm's required filings with the Board in the first instance for information as to where the firm's offices are located, though two commenters suggested that the Board look beyond such filings to ascertain or validate the location of a

firm's offices. As previously noted, the Board retains the ability to consider other relevant and reliable information, including the information identified by the commenters, when determining where a firm's offices are located.

One commenter requested guidance about the application of the proposed rule when a firm that is headquartered in a cooperative jurisdiction uses local personnel in a noncooperative jurisdiction to perform an audit for an issuer located in the noncooperative jurisdiction. In such a circumstance, the firm could not be subject to a jurisdiction-wide determination under subparagraph (a)(1) because it is not headquartered in a noncooperative jurisdiction, but it could be subject to a determination under subparagraph (a)(2) if it has an office in the noncooperative jurisdiction.

#### Timing of Board Determinations

Subparagraph (a)(3) of the proposed rule addresses the timing of the Board's determinations under the HFCAA. Promptly after the Board's proposed rule becomes effective upon the Commission's approval, the Board will make any determinations under subparagraph (a)(1) or (a)(2) that are appropriate. Thereafter, the Board will consider, at least annually, whether changes in facts and circumstances support any additional determinations under subparagraph (a)(1) or (a)(2). If so, the Board will make such additional determinations, as and when appropriate, to allow the Commission on a timely basis to identify covered issuers in accordance with the Commission's rules.

The Board is well positioned to assess the facts and circumstances surrounding its inspections and investigations and gauge whether and when a determination is appropriate under the proposed rule. The relevant circumstances in a jurisdiction can change quickly and unpredictably because foreign authorities can enact or amend laws, issue or modify rules or regulations, change their interpretation or application of those laws and rules, and otherwise take new positions with limited or no notice. The proposed rule allows the Board to make new determinations whenever appropriate, while acknowledging that the Board's timing will be informed by the Commission's process for timely identifying covered issuers and also establishing that the Board will consider whether new determinations are warranted at least once each year.

When considering whether changed facts or circumstances provide a sufficient basis for a new Board

<sup>87</sup> The HFCAA authorizes the Board to make determinations as to firms having a "branch" or "office" in a foreign jurisdiction where the Board is unable to inspect or investigate completely because of a position taken by an authority in that jurisdiction. HFCAA § 2(i)(2)(A), 15 U.S.C. 7214(i)(2)(A). Unlike in other contexts (such as banking), however, there is no commonly recognized distinction between a "branch" and an "office" with respect to accounting firms. Accordingly, the proposed rule refers only to an "office," which is a term commonly used by the Board in connection with its oversight programs. A majority of the commenters who addressed this rationale agreed with it.

<sup>88</sup> Firms are required to identify all of their offices when they first register with the Board (in Item 1.5 of the application for registration on Form 1) and annually thereafter (in Item 5.1 of the annual report on Form 2).

<sup>89</sup> The phrase "Particular Registered Firm in a Foreign Jurisdiction" has been revised to "Particular Registered Firm With an Office in a Foreign Jurisdiction" to mirror more closely the text of subparagraph (a)(2), create a parallel structure between the titles of subparagraphs (a)(1) and (a)(2), and provide a clearer contrast between the scope of those two subparagraphs.

determination, the Board may confront a number of different scenarios. It is not possible to identify with specificity all the developments that might lead to a new determination, but they could include the enactment of a new law or regulation, a change in the interpretation or the application of an existing law or regulation, the termination of or failure to perform under an existing cooperative arrangement, and the failure to take or renew an administrative action necessary to facilitate the Board's oversight. The Board's experience in a particular inspection or investigation also could supply the grounds for a new Board determination in accordance with the proposed rule.

The Board adopted subparagraph (a)(3) substantially as proposed.<sup>90</sup> The majority of commenters who addressed this issue expressed support for the Board's approach to the timing of determinations.

One commenter emphasized that the Board's approach should be sufficiently flexible so that Board determinations do not conflict with the language and intent of the HFCAA. The Board believes that subparagraph (a)(3) provides such flexibility, insofar as it provides that the Board will make any appropriate determinations promptly after the proposed rule becomes effective and thereafter will make additional determinations as and when appropriate to allow the Commission to identify covered issuers on a timely basis.

Another commenter suggested that the Board require firms to file special reports on Form 3 to apprise the Board of headquarters or office location changes. Such changes already are reported to the Board annually on Form 2. The Board does not believe that a new Form 3 reporting obligation should be imposed. If a firm opts to expose its issuer clients to the potential consequences of the HFCAA by moving the firm's headquarters to a jurisdiction that is subject to a jurisdiction-wide determination, such a change could be captured through the Board's current reporting procedures.<sup>91</sup> Moreover, if a

firm that is headquartered outside a noncooperative jurisdiction opens an office in a noncooperative jurisdiction, the Board would not anticipate making a determination as to that particular firm under subparagraph (a)(2) without evidence that the Board's ability to inspect and investigate the firm completely has become restricted as a result of the opening of the new office. Lastly, if a firm that is subject to a Board determination moves its headquarters out of or closes all of its offices in a noncooperative jurisdiction, the firm is required to notify the Board within five days of that development pursuant to subparagraph (e)(4) of the proposed rule, discussed below.

#### Factors for Board Determinations

Paragraph (b) provides factors for Board determinations under the proposed rule. When determining whether it can "inspect or investigate completely" under subparagraph (a)(1) as to a particular jurisdiction or subparagraph (a)(2) as to a particular firm, the Board will assess whether "the position taken by the authority (or authorities)" in the jurisdiction "impairs the Board's ability to execute its statutory mandate with respect to inspections or investigations," as detailed above.

To make this assessment, the Board will evaluate three factors, which correlate to the three principles that guide the Board's approach to international cooperation. These factors embody the access the Board needs, and already experiences nearly worldwide, to fulfill its inspection and investigation mandates. Conceding on these factors in particular jurisdictions would dilute the Board's oversight in a selective, unequal manner and would be detrimental to the PCAOB's mission. In other words, this framework promotes a level playing field for U.S. and non-U.S. registered firms, in accordance with the Act's directive that non-U.S. registered firms are subject to the Act and the Board's rules in the same manner and to the same extent as U.S. registered firms.

No commenter suggested other benchmarks or factors that the Board should employ when making determinations, and one commenter stated that the factors set forth in paragraph (b) are appropriate and clear. The Board adopted paragraph (b) as proposed, except for one addition to

board, or other authority that issued the new license or certification. *See id.* And if a firm changes the jurisdiction under the law of which it is organized, the firm may file a Form 4 to succeed to the registration status of its predecessor. *See* PCAOB Rule 2109, *Procedure for Succeeding to the Registration Status of a Predecessor*.

subparagraph (b)(2)'s second factor, as discussed below.

The first factor is "the Board's ability to select engagements, audit areas, and potential violations to be reviewed or investigated." The ability to make such selections is critical to the Board's oversight activities and is embedded in its statutory mandate.<sup>92</sup> This factor would encompass situations in which a foreign authority takes the position that certain engagements, or certain parts of engagements, cannot be reviewed during an inspection, or that the Board cannot decide when (*i.e.*, in which inspection year) certain engagements will be reviewed. It also would encompass situations in which a foreign authority takes the position that the Board cannot decide what potential violations it will investigate. No commenter expressed the view that this factor is unclear or inappropriate or sought further guidance about it.

The second factor is "the Board's timely access, and the ability to retain and use, any document or information (including through conducting interviews and testimony) in the possession, custody, or control of the firm(s) or any associated persons thereof that the Board considers relevant to an inspection or investigation." The Board's access to firm personnel, documents, and information is pivotal to its inspections and investigations, and is built into its mandate to oversee the audits of issuers that avail themselves of the U.S. capital markets.<sup>93</sup>

One commenter suggested that the Board add "timely" to this factor so that it refers to "timely access," and, after consideration, the Board has made that revision. The Board agrees with the commenter that the Board cannot inspect or investigate completely if its access to documents or information is not timely. Unreasonable delays in obtaining documents or information hinder the Board's ability to execute its statutory mandate<sup>94</sup> and therefore its ability to protect the interests of investors and further the public interest. No other commenter made any suggestions regarding this factor, and no commenter asserted that this factor is

<sup>90</sup> For clarity, in the second sentence of the subparagraph, "changes in the facts and circumstances" has been changed to "changes in facts and circumstances."

<sup>91</sup> For instance, whenever the business mailing address of a firm's primary contact with the Board changes, the firm must file a special report on Form 3 that supplies the new address in Item 7.2. *See* PCAOB Rule 2203, *Special Reports*. Additionally, if a firm obtains a new license or certification to engage in the business of auditing or accounting from a governmental or regulatory authority, the firm must file a special report on Form 3 that identifies, in Item 6.2, the name of the state, agency,

<sup>92</sup> *See, e.g.*, Sections 104(d) and 105(b)(1) of the Act.

<sup>93</sup> *See, e.g.*, Sections 104(d) and 105(b)(2) of the Act.

<sup>94</sup> *See, e.g.*, Section 104(b) of the Act (specifying inspection frequency requirements); Section 105(b)(2)(B) of the Act (authorizing the Board to require production of audit work papers and other documents or information); PCAOB Rule 5103(b) (providing that requests for documents or information shall set forth "a reasonable time . . . for production").

unclear or inappropriate or sought further guidance about it.

The third factor is “the Board’s ability to conduct inspections and investigations in a manner consistent with the provisions of the Act and the Rules of the Board, as interpreted and applied by the Board.” This provision captures all of the other aspects of the Board’s inspection and investigation mandates not already subsumed in the first and second factors. That includes the Board’s ability to satisfy inspection frequency requirements,<sup>95</sup> to identify potentially violative acts during inspections,<sup>96</sup> to impose sanctions for noncooperation with an investigation,<sup>97</sup> and to share information with the Commission and other regulators.<sup>98</sup> No commenter indicated that this factor is unclear or inappropriate or sought further guidance about it.

Importantly, these three factors do not function as separate prerequisites for a Board determination. Instead, impairment in any one respect may be sufficient under the circumstances to support a Board determination. To underscore the disjunctive nature of this three-factor analysis, the proposed rule provides that the Board will assess whether its ability to execute its mandate has been impaired in “one or more” of these three respects. No commenter objected to, or expressed concerns about, this approach.

Additionally, to make a determination under the proposed rule, the Board does not need to conclude that it has been impaired as to both its inspections and its investigations. The HFCAA authorizes the Board to make a determination if the Board is unable to inspect “or” investigate completely, and the proposed rule uses “or” in similar fashion: It is enough that the Board is impaired in its ability to execute its mandate with respect to either inspections or investigations. This approach is consistent with the HFCAA, and no commenter suggested otherwise.

#### Basis for Board Determinations

Paragraph (c) of the proposed rule addresses the basis for a Board determination. This provision establishes, first and foremost, that when assessing whether its ability to execute its mandate has been impaired, the Board may consider “any documents or information it deems relevant.” From there, the proposed rule specifies, for the avoidance of doubt,

three non-exclusive categories of documents and information that the Board can rely upon when making a determination. No commenter objected to this approach or expressed concern about the three non-exclusive categories identified in the proposed rule, and one commenter stated that paragraph (c) provides adequate and substantive guidance. The Board adopted paragraph (c) as proposed.

Subparagraph (c)(1) states that the Board may consider a foreign jurisdiction’s laws, statutes, regulations, rules, and other legal authorities; in other words, the black-letter law of the foreign jurisdiction (and any political subdivisions thereof) in all of its varying forms. The Board also may consider relevant interpretations of those laws, whether by the promulgating authority or others, as well as real-world applications of those laws.

Subparagraph (c)(2) provides that the Board may consider the entirety of its efforts to reach and secure compliance with agreements with foreign authorities in the jurisdiction. In so doing, the Board can take into account whether an agreement was reached, the terms of any such agreement, and the foreign authorities’ interpretation of and performance under any such agreement.

Subparagraph (c)(3) recognizes that the Board may consider its experience with foreign authorities’ other conduct and positions relative to Board inspections or investigations. This allows the Board to consider the totality of a foreign authority’s prior conduct and positions in all contexts, including public and private statements made, positions asserted, and actions taken. This provision also may encompass circumstances where a foreign authority precipitously changes its position regarding PCAOB access without making any change to its laws or demanding any form of cooperative agreement.

Together, these provisions establish that the Board can consider any relevant information (including, but not limited to, the three categories of information discussed above) when making a determination. As a corollary, paragraph (d) of the proposed rule establishes that the Board’s determination need not depend on the Board’s “commencement of, but inability to complete, an inspection or investigation.” The Board should not be expected to attempt to initiate inspections or investigations in a foreign jurisdiction that rejects the guiding principles for international cooperation, because such futile efforts would not advance the Board’s mission of protecting investors and furthering the public interest in the preparation of

informative, accurate, and independent audit reports. No commenter challenged the Board’s reasoning or expressed the view that the Board must initiate an inspection or investigation as a prerequisite to making a determination under the HFCAA. Nor did any commenter indicate that the approach described in paragraph (d) is inappropriate. The Board adopted paragraph (d) as proposed.

#### Form and Publication of Board Determinations

##### Board Reports to the Commission

The HFCAA does not specify how the Board should communicate its determinations to the Commission. Subparagraph (e)(1) of the proposed rule establishes that process.

When the Board makes a determination, whether as to a particular jurisdiction under subparagraph (a)(1) or a particular firm under subparagraph (a)(2), the Board’s determination will be issued in the form of a report to the Commission.<sup>99</sup> Such a reporting process is authorized under Sections 101(c)(5), 101(g)(1), and 101(f)(6) of the Act.<sup>100</sup>

The Board’s report will describe its assessment of whether the position taken by the foreign authority (or authorities) impairs the Board’s ability to execute its mandate with respect to inspections or investigations. The report will analyze the relevant factor(s) set forth in paragraph (b) and describe the basis for the Board’s conclusions. The Board will identify the firm(s) subject to the Board’s determination in two ways: by the name under which the firm is registered with the Board, and by the firm’s identification number with the Board. No commenter identified any additional information that should be included in the Board’s reports to the Commission.

The Board adopted subparagraph (e)(1) as proposed but with one modification: The Board will identify the firm(s) to which a determination applies in an appendix to the Board’s report. Identifying such firms in a

<sup>99</sup> The Board will decide whether to conduct a public or non-public meeting to consider a potential determination under the HFCAA in accordance with the PCAOB bylaws. See Bylaw 5.1, *Governing Board Meetings*.

<sup>100</sup> See Section 101(c)(5) of the Act (the Board shall “perform such other duties or functions as the Board . . . determines are necessary or appropriate . . . to carry out this Act”); Section 101(g)(1) of the Act (the Board’s rules “shall . . . provide for . . . the performance of its responsibilities under this Act”); Section 101(f)(6) of the Act (the Board is authorized to “do any and all . . . acts and things necessary, appropriate, or incidental to . . . the exercise of its obligations . . . imposed” by the Act).

<sup>95</sup> See Section 104(b) of the Act.

<sup>96</sup> See Section 104(c)(1) of the Act.

<sup>97</sup> See Section 105(b)(3)(A) of the Act.

<sup>98</sup> See Sections 104(c)(2) and 105(b)(4)–(5) of the Act.

separate appendix will facilitate the Board's efforts to keep the list of firms subject to the determination current, as discussed below.

#### Publication of Board Reports

Promptly after the Board issues a report to the Commission, a copy of the report will be made publicly available on the PCAOB's website. The Board expects that a copy of the report ordinarily will be prominently featured on the Board's website on or about the same day the Board issues its report to the Commission.

Subparagraph (e)(2) of the proposed rule specifies, however, that the content of the Board's publicly available report will be subject to two limitations. First, the Board will be bound by Section 105 of the Act, which provides, in pertinent part, that "all documents and information prepared or received by or specifically for the Board . . . in connection with an inspection . . . or with an investigation . . . shall be confidential . . . , unless and until presented in connection with a public proceeding or released" in accordance with Section 105(c) of the Act.<sup>101</sup> If the Board's report contains material encompassed by Section 105(b)(5)(A) of the Act, such material will be redacted from the publicly available version of the report posted on the PCAOB's website, in accordance with the Act.

Second, while the Board does not anticipate that such situations will frequently arise, the version of the Board's report posted on the PCAOB's website will be redacted if it contains proprietary, personal, or other information protected by applicable confidentiality laws. In this respect, the proposed rule aligns with the Act's treatment of registration applications and annual reports filed with the Board, which the Board may make publicly available subject to "applicable laws relating to the confidentiality of proprietary, personal, or other information."<sup>102</sup>

Commenters generally supported redacting from the Board's publicly available reports any information that is subject to applicable confidentiality laws. One commenter suggested that redaction should not be limited to information covered by applicable confidentiality laws, but rather should be based on broader concepts of confidentiality. That commenter offered one example of such a concept, but that example—accountants' professional responsibilities of confidentiality—does not apply to the Board's performance of

its oversight functions. Another commenter similarly suggested that redaction should extend to all confidential information whether explicitly covered by confidentiality laws or not, but that commenter did not suggest how to define this broader concept of confidential information or what categories of information it would encompass. Neither of these commenters identified any specific type of relevant information that is not subject to a confidentiality law but is nevertheless worthy of protection under a broader view of confidential information.

Besides one minor revision unrelated to redaction,<sup>103</sup> the Board adopted subparagraph (e)(2) as proposed. The Board believes that it is appropriate to limit redaction to confidential information protected by law. That approach comports with the Board's congressionally mandated treatment of registration applications and annual reports, which the Board also has extended to other reports filed with the Board. This approach also is more readily administrable than one that relies instead on broader, undefined concepts of confidentiality.

#### Transmittal of Board Reports to Subject Firms

The Board revised the proposed rule to add a new provision regarding the transmittal of reports to firms that are subject to a determination. While some commenters stated that posting Board reports on the Board's website would give sufficient notice of Board determinations to such firms, other commenters disagreed, and the Board has concluded that it would be prudent to transmit reports to those firms.

Subparagraph (e)(3) provides that promptly after the Board issues a report to the Commission under subparagraph (e)(1), a copy of the report will be sent by electronic mail to each registered public accounting firm that is listed in the appendix to that report (*i.e.*, each firm as to which the determination applies). The Board expects that the report will be transmitted to the subject firm(s) by electronic mail after it has been posted on the Board's website, though both actions will take place promptly after the issuance of the report. Such reports will be redacted to the extent required by confidentiality laws, and the electronic mail will be directed to the electronic mail address

of the firm's primary contact with the Board.<sup>104</sup>

Two commenters suggested that the Board provide non-public advance notice of a forthcoming determination to firms that would be subject to that determination. One of those commenters indicated that firms could use this advance notice to initiate discussions with their issuer audit clients about the Board's forthcoming determination.

The Board does not believe that it is appropriate to provide non-public advance notice to firms. A firm headquartered in a noncooperative jurisdiction and performing audit work that subjects the firm to the PCAOB inspection requirement should know if it has not been inspected due to the PCAOB's inability to inspect such firm or firms in that jurisdiction.<sup>105</sup> Furthermore, as described above, the Board has long taken efforts to make known the access challenges it faces in certain jurisdictions. Although those disclosures are distinct from determinations under the proposed rule and predate the HFCAA's enactment, they underscore the Board's commitment to transparency about its oversight access. And if a firm-specific obstacle to Board inspections or investigations were to arise that might warrant a determination as to a particular registered firm pursuant to subparagraph (a)(2), the Board expects that it would have engaged with that firm about the Board's inability to inspect or investigate the firm completely before such a determination would be made.

In addition, providing non-public advance notice of a Board determination to firms would create information asymmetry in the marketplace: A forthcoming Board determination would be known to firms and to anyone with whom the firm elects to share that information (including not only the firm's issuer clients' management, but also potentially the issuers' directors, the issuers' outside counsel and other professional advisors, foreign government officials, and others), while

<sup>104</sup> When applying to register with the Board, firms provide an electronic mail address for their primary contact with the Board in Item 1.3.7 of Form 1. Thereafter, firms confirm the electronic mail address for their primary contact with the Board annually in Item 1.3 of Form 2. If that electronic mail address changes, the firm must notify the Board within 30 days of the new electronic mail address for its primary contact with the Board in Item 7.2 of Form 3.

<sup>105</sup> See also, *e.g.*, SEC Exchange Act Release No. 91364, at 26 (noting "a highly similar type and pattern of disclosure regarding the PCAOB's inability to inspect those firms" in Item 3 of Form 20-F and in Item 1A of Form 10-K).

<sup>101</sup> Section 105(b)(5)(A) of the Act.

<sup>102</sup> Section 102(e) of the Act.

<sup>103</sup> For simplicity, the phrase "Board report containing a determination pursuant to subparagraph (a)(1) or (a)(2)" has been changed to "Board report pursuant to subparagraph (e)(1)."

the investing public would not be privy to the same information. The Board does not believe it would be in the public interest or the interests of investors to selectively preview its determinations in such a manner.

Several commenters also suggested that the Board establish a rule-based mechanism that would allow firms to submit information to the Board regarding a determination. Some of those commenters recommended that the Board provide by rule for such a submission process before a Board determination takes effect, while others expressed concern that such an approach could delay the timely implementation of the HFCAA. No commenter, however, identified any type of information that a firm might have that would be both relevant to a Board determination and previously unknown to the Board.

Because the Board believes that firms are unlikely to have new and relevant information regarding a determination, the Board is not establishing a rule-based process for firms to make such submissions. Board determinations turn on positions taken by authorities in foreign jurisdictions, and such positions, by virtue of having previously been “taken” by a foreign authority, necessarily will be known to the Board already. Indeed, the Board has extensive experience in this area and, over more than a decade, has engaged significantly with foreign authorities and registered firms regarding inspections and investigations of non-U.S. firms. Therefore, the Board knows, and will timely learn, relevant information about its ability to conduct inspections and investigations abroad. The Board’s history of engagement and negotiations regarding such inspections and investigations is detailed above, and no commenter disputed the Board’s description of that history.

By the same token, any Board determination would be based on the Board’s judgment as to whether the extent of access available to it impairs its ability to conduct oversight in any of the three respects identified in paragraph (b). Consequently, the Board does not believe that firms will be able to contribute meaningfully to the mix of information available to the Board regarding foreign authorities’ positions or the Board’s experience-driven assessment of paragraph (b)’s three factors. Should a firm wish to communicate with the Board about its inspection or investigation experience, however, it can do so through existing channels for communicating with the Board’s inspection and enforcement staff.

#### Updating the Appendix to a Board Report

Subparagraph (e)(4) addresses the Board’s process for determining that the list of firms subject to a determination remains accurate. A few commenters expressed concern about potential developments that could render such a list inaccurate, and the Board believes that it is prudent to establish a process in the proposed rule to ensure the list is appropriately updated and accurate.

As provided in subparagraph (e)(1), the list of firms subject to a determination will be contained in an appendix to the Board’s report. For a jurisdiction-wide determination under subparagraph (a)(1), the appendix will provide, for each firm, the name under which it is registered with the Board, its identification number with the Board, and the jurisdiction in which its headquarters is located. For a determination as to a particular firm under subparagraph (a)(2), the appendix will provide the name under which the firm is registered with the Board, its identification number with the Board, and the location of the office(s) the firm maintains in the foreign jurisdiction whose authorities have taken a position that results in the Board being unable to inspect or investigate the firm completely.

Subparagraph (e)(4) requires firms identified in an appendix to notify the PCAOB Secretary of any changes to the firm’s information in the appendix within five days of such a change.<sup>106</sup> Firm names, identification numbers, headquarters locations, and office locations can change, and this requirement ensures that the Board will be alerted promptly to updated information.<sup>107</sup> Instructions regarding how to notify the Secretary of such a change will be provided in the appendix.

Subparagraph (e)(4) provides that the Board may issue an updated appendix at any time. This allows the Board to update its appendix to reflect changes reported by firms as required by

subparagraph (e)(4). It also enables the Board to correct discrepancies or reflect changes identified by the Board or its staff through other means.<sup>108</sup> An updated appendix will bear the date on which it was issued by the Board.

The Board’s issuance of an updated appendix would not constitute a reassessment of the Board’s underlying determination. In other words, the Board can update an appendix without reanalyzing the three factors identified in paragraph (b). Whenever the Board issues an updated appendix, it will transmit that appendix to the Commission, make it publicly available in accordance with subparagraph (e)(2), and send it to firms that are identified in the appendix in accordance with subparagraph (e)(3).

#### Effective Date and Duration of Board Determinations

Paragraph (f) provides that a Board determination becomes effective on the date the Board issues its report to the Commission. Most commenters expressed support for this timing, though one commenter suggested that this timing would be appropriate only if firms received advance notice of a determination, and another commenter suggested that the Board delay the effectiveness of its determinations (*e.g.*, for 120 days) so that issuers have time to understand and plan for them.

The Board adopted paragraph (f) substantially as proposed.<sup>109</sup> For many of the same reasons that the Board does not believe that firms should receive advance notice of Board determinations (as discussed above), the Board does not believe that the effectiveness of its determinations should be delayed. Furthermore, delaying the effectiveness of a determination could frustrate the objectives of the HFCAA and, in the Board’s view, impair the Commission’s ability to identify covered issuers on a timely basis pursuant to its rules.

One commenter requested clarification regarding the date of issuance of a Board report. The date of issuance will be the date that appears on the report, which will correspond to the date upon which the Board’s report is transmitted to the Commission.

<sup>106</sup> In practice, this five-day period would span at least seven calendar days. See PCAOB Rule 1002, *Time Computation* (providing that Saturdays, Sundays, and federal legal holidays are excluded from the computation of time when a prescribed period of time in a Board rule is seven days or less).

<sup>107</sup> For example, if a firm changes its name while remaining the same legal entity, the firm has 30 days to notify the Board of its name change in Item 7.1 of Form 3. But if a firm changes its name while also changing its legal entity due to a change to its legal form of organization or as the result of a business combination, the firm may (but is not required to) file a Form 4 that, among other things, would notify the Board of the name change in Item 1.1, and that filing would be due 14 days after the change or business combination, unless the Board permits the firm to file its form out of time.

<sup>108</sup> For instance, the list of firms in the appendix could be reduced if a firm withdraws from registration or has its registration revoked, and could be expanded if a registered firm moves its headquarters to a jurisdiction that is the subject of a jurisdiction-wide determination.

<sup>109</sup> For simplicity, at the beginning of the paragraph, “When the Board makes a determination pursuant to subparagraph (a)(1) or (a)(2), the Board’s determination becomes effective” has been replaced by “A determination pursuant to subparagraph (a)(1) or (a)(2) becomes effective.”

Paragraph (g) addresses the duration of Board determinations. The Board adopted paragraph (g) substantially as proposed,<sup>110</sup> save for one conforming change. As first proposed, the proposed rule provided that a Board determination would remain in effect “unless and until” it was modified or vacated. As discussed below, however, the Board has elected to reassess at least annually each determination that is in effect and to issue, at the conclusion of each reassessment, a report reaffirming, modifying, or vacating the determination. To conform to that approach, paragraph (g) has been revised to provide that a Board determination will remain in effect until it is reaffirmed, modified, or vacated by the Board.

#### Reassessment of Board Determinations

As first proposed, paragraph (h) created a two-step process through which the Board would annually monitor the continued justification for a Board determination. First, the Board would consider whether changes in facts and circumstances warrant a reassessment of a determination that is in effect. Then, if the Board concludes that a reassessment is warranted, the Board would analyze the three factors identified in paragraph (b) and decide whether to leave its determination undisturbed or issue a new report modifying or vacating the determination. Apart from that annual process, the Board also could reassess a determination on its own initiative or at the Commission’s request at any time.

Commenters generally supported that proposed two-step annual process. A few commenters suggested that the result of a reassessment should be made public in all circumstances, even when a determination is left undisturbed, and one commenter indicated that such public reporting could provide audit firms and issuers with more detailed guidance and transparent information. Some commenters suggested that firms should be able to request reevaluation of a determination outside of the annual cycle, with one commenter asking the Board to confirm that it would reassess a determination anytime there was a potentially material development in the facts and circumstances.

The Board has revised paragraph (h) to reduce the two-step process to a one-step process by eliminating the “annual consideration of changed facts and circumstances” contemplated in the proposed rule. Instead of requiring the

Board to conduct a threshold inquiry each year to decide whether changes in facts and circumstances merit reassessment of a determination, the proposed rule requires the Board to annually reassess each determination that is in effect. The Board believes that annual reassessment best aligns with the HFCAA’s annual cycle, which includes the Commission’s identification of covered issuers based on the filing of annual reports and its designation of non-inspection years.<sup>111</sup>

Apart from its mandatory annual reassessments, the Board, on its own initiative or at the Commission’s request, may reassess a determination at any time. It is not possible to specify every development that might prompt the Board to reassess a determination outside of the annual reassessment cycle. In certain circumstances, the withdrawal of a law or the execution of a cooperative agreement might suffice, if, for example, the law or the absence of an agreement were the sole reason why the Board’s access was impaired in one or more of the respects identified in paragraph (b). However, as a general matter, when a determination derives from the Board’s prolonged inability to complete inspections or investigations in a particular jurisdiction or of a particular firm, the Board does not anticipate modifying or vacating such a determination—even if a cooperative agreement is in place—until it has concluded that the foreign authority has taken, and the Board can reasonably conclude that the authority will maintain, new positions that respond satisfactorily to the Board’s access needs with respect to each of the factors identified in paragraph (b). In such instances of prolonged lack of access, the Board would expect to conclude inspections or investigations in that jurisdiction or of that firm before modifying or vacating a determination. The conclusion of an inspection or investigation, however, is not necessarily conclusive evidence that the conditions preventing the Board from inspecting or investigating completely firms located in the foreign jurisdiction have been resolved.

Together, the proposed rule’s framework of mandatory annual reassessment and discretionary off-cycle reassessment gives the Board the opportunity to reassess a determination whenever facts and circumstances warrant, and will help ensure that the Commission’s actions under the HFCAA are based on Board determinations that reflect the current status of the Board’s ability to inspect and investigate firms

completely. When conducting a reassessment, whether annual or off-cycle, the Board will reanalyze the three factors identified in paragraph (b), and at the conclusion of that reassessment, the Board will reaffirm, modify, or vacate its determination.

Two commenters suggested that the Board allow firms to request reevaluation of a determination outside of the Board’s annual reassessment process. One commenter further suggested that reevaluation requests could be based on a triggering event, but did not provide any examples of such an event or explain how a firm would have knowledge of such an event that the Board would lack. As explained above, the Board believes that firms are unlikely to have new, relevant information about positions taken by foreign authorities vis-à-vis the Board, and firms already have other channels through which they can communicate with the Board’s staff about inspection- and investigation-related developments. Furthermore, even without a rule-based mechanism through which firms could request reevaluation, the Board will reassess determinations to which any firm is subject at least once a year.

One commenter suggested that the Board allow “jurisdictions” to request reevaluation of determinations at any time. That commenter was not a foreign authority; indeed, no foreign authority submitted a comment asking for the ability to request reevaluation. Nor did the commenter explain why foreign authorities cannot communicate with the Board through existing channels. The Board believes that those customary channels for communication with foreign authorities, together with the Board’s annual mandatory reassessments and discretionary off-cycle reassessments, suffice to provide the Board appropriate information to reexamine determinations as and when appropriate.

#### Reaffirmed, Modified, and Vacated Board Determinations

Paragraph (i) addresses reaffirmed, modified, and vacated Board determinations. The Board adopted paragraph (i) with several conforming changes that align paragraph (i) with other revisions to the proposed rule, including revisions regarding appendices to Board reports, the transmittal of Board reports by electronic mail, and annual reassessment of determinations that are in effect.

When the Board reaffirms, modifies, or vacates a determination, it will issue a report to the Commission describing its assessment and the basis for

<sup>110</sup>For simplicity, at the beginning of the paragraph, “A determination made by the Board” has been changed to “A determination.”

<sup>111</sup>HFCAA § 2(i)(1)–(2), 15 U.S.C. 7214(i)(1)–(2).



reaffirming, modifying, or vacating the determination. In the case of a reaffirmed or modified determination, the Board will update the appendix to the report that identifies the firm(s) to which the determination applies. A copy of the report will be posted on the PCAOB's website and sent by electronic mail to each firm's primary contact with the Board, subject to the confidentiality limitations described above in connection with subparagraphs (e)(2) and (e)(3).

A reaffirmed or modified determination, or the vacatur of a determination, will become effective on the date that the Board issues its report to the Commission. A reaffirmed or modified determination will be subject to reassessment under paragraph (h): It must be reassessed at least annually; it may be reassessed at any time; and the Board's reassessment will consider the three factors identified in paragraph (b) and result in reaffirmation, modification, or vacatur. A reaffirmed or modified determination will remain in effect until it is reaffirmed, modified, or vacated.

#### *D. Economic Considerations*

The Board is mindful of the economic impacts of its rulemaking. This section discusses economic considerations related to the proposed rule, including the need for the rulemaking; a description of the baseline for evaluating the economic impacts of the proposed rule; consideration of the benefits, costs, and unintended consequences of the proposed rule; and alternatives considered by the Board.

The proposed rule does not require "mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements" of issuers, nor does it impose any "additional requirements" on auditors.<sup>112</sup> Accordingly, the Board has concluded that Section 103(a)(3)(C) of the Act does not apply to this rulemaking, and no commenter suggested otherwise.

#### *Need for Rulemaking*

As discussed in Section C above, the HFCAA does not expressly require the Board to adopt a rule governing the determinations it makes under the statute. Rather, the HFCAA gives the Board discretion regarding the procedure for making those determinations and the content and format of the Board's reporting to the Commission. The Board elected to pursue a rulemaking to bring transparency and consistency to its determinations. Specifically, the Board believes that a rule would inform investors, registered firms, issuers, audit committees, foreign authorities, and the public at large as to how the Board will perform its functions to satisfy its obligations under the statute. It also would promote consistency in the Board's process regarding determinations.

#### *Baseline*

The Board has evaluated the potential benefits, costs, and unintended consequences of the proposed rule relative to a baseline that consists of the current regulatory framework and current market practices. Although the HFCAA requires the Board to make a determination about which audit firms located in a foreign jurisdiction it is unable to inspect or investigate completely because of a position taken by one or more authorities in that jurisdiction, the HFCAA does not expressly require the Board to adopt a rule governing the determinations it makes under the statute. Moreover, the PCAOB website has long identified the jurisdictions in which the Board lacks inspection access, as well as the registered firms located in those jurisdictions.<sup>113</sup> Measured against this baseline, the proposed rule builds on existing PCAOB practices and provides a framework for the Board's determinations under the HFCAA and, hence, should have limited economic impacts incremental to the impacts of the HFCAA and the Commission's actions to implement the HFCAA.

Under the HFCAA, issuers that retain firms that are subject to a Board determination to issue audit reports on

their financial statements must make certain disclosures and submissions and, eventually, if certain conditions persist, the securities of those issuers may be subject to a prohibition on trading. The Commission has adopted interim final amendments to Forms 20-F, 40-F, 10-K, and N-CSR to implement the disclosure and submission requirements of the HFCAA.<sup>114</sup> Other aspects of the HFCAA, including the trading prohibition, will be addressed in subsequent Commission actions.<sup>115</sup> The economic impact of these aspects of the HFCAA, while tied to the Board's determinations about which audit firms it is unable to inspect or investigate completely, will depend on the implementation choices made by the Commission in carrying out its mandate under the HFCAA and thus are not considered as part of the economic analysis with respect to this rulemaking.

The baseline also takes into consideration the current international reach of the Board's oversight mandate. As of June 30, 2021, 851 non-U.S. firms, headquartered in 90 foreign jurisdictions, were registered with the Board.<sup>116</sup> Out of those 851 non-U.S. registered firms, 202 issued at least one audit report on financial statements filed by an issuer with the Commission in the 12-month period ended June 30, 2021, and, altogether, they issued 1,260 audit reports during that 12-month period.<sup>117</sup>

Exhibit 1 reports the jurisdictions with the highest number of audit reports issued by non-U.S. registered firms on financial statements filed by issuers with the Commission during the 12-month period ended June 30, 2021. The top 15 jurisdictions account for 84% of all audit reports issued by non-U.S. registered firms on financial statements filed by issuers during the 12-month period ended June 30, 2021.

<sup>114</sup> See SEC Exchange Act Release No. 91364. The interim final rule amendments became effective on May 5, 2021.

<sup>115</sup> See *id.*

<sup>116</sup> Source: PCAOB Registration, Annual, and Special Reporting ("RASR") System and Audit Analytics.

<sup>117</sup> If a firm issued more than one audit report on financial statements filed by the same issuer during the 12-month period ended June 30, 2021, then only the most recent audit report is counted.

<sup>112</sup> Section 103(a)(3)(C) of the Act.

<sup>113</sup> For an overview of this historical practice, see, for example, footnote 62.

**Exhibit 1. Top Fifteen Non-U.S. Jurisdictions by Number of Audit Reports Issued by Non-U.S. Registered Firms on Financial Statements Filed by Issuers During the 12-Month Period Ended June 30, 2021<sup>118</sup>**

Jurisdiction	Audit Reports Issued by Non-U.S. Registered Firms on Issuer Financial Statements		Market Capitalization		Number of Non-U.S. Registered Firms		Number of Non-U.S. Registered Firms Issuing Audit Reports on Issuer Financial Statements	
	#	%	\$ Billions	%	#	%	#	%
Canada	358	28.4%	1,979	15.9%	36	4.2%	24	11.9%
China (Excluding Hong Kong)	169	13.4%	1,709	13.7%	36	4.2%	9	4.5%
Israel	155	12.3%	231	1.8%	21	2.5%	10	5.0%
United Kingdom	76	6.0%	1,639	13.1%	47	5.5%	7	3.5%
Hong Kong	50	4.0%	734	5.9%	28	3.3%	8	4.0%
Brazil	41	3.3%	584	4.7%	18	2.1%	7	3.5%
India	28	2.2%	362	2.9%	66	7.8%	11	5.4%
Singapore	27	2.1%	155	1.2%	25	2.9%	8	4.0%
Malaysia	25	2.0%	3	0.0%	18	2.1%	3	1.5%
Argentina	24	1.9%	112	0.9%	16	1.9%	4	2.0%
France	24	1.9%	296	2.4%	24	2.8%	5	2.5%
Switzerland	23	1.8%	588	4.7%	6	0.7%	5	2.5%
Greece	22	1.7%	10	0.1%	8	0.9%	3	1.5%
Germany	19	1.5%	316	2.5%	31	3.6%	4	2.0%
Mexico	17	1.3%	191	1.5%	20	2.4%	6	3.0%
<b>+ Other Non-US Jurisdictions</b>	<b>202</b>	<b>16.0%</b>	<b>3,563</b>	<b>28.6%</b>	<b>451</b>	<b>53.0%</b>	<b>88</b>	<b>43.6%</b>
<b>Total of All Non-US Jurisdictions</b>	<b>1,260</b>	<b>100%</b>	<b>12,471</b>	<b>100%</b>	<b>851</b>	<b>100%</b>	<b>202</b>	<b>100%</b>

Source: RASR, Audit Analytics, and Standard & Poor's.

As discussed in Section C above, over the years, the Board has been able to work effectively with authorities in foreign jurisdictions to fulfill its mandate to oversee registered firms located outside the United States. With rare exceptions, foreign audit regulators have cooperated with the Board and allowed it to exercise its oversight authority as it relates to registered firms located within their respective jurisdictions. Authorities in a limited number of foreign jurisdictions, however, have taken positions that deny the Board access for oversight activities. The PCAOB's website identifies the

jurisdictions that currently deny the Board such access.<sup>119</sup>

Considerations of the Benefits, Costs, and Unintended Consequences

Compared to the baseline of no PCAOB rulemaking, the proposed rule would have incremental benefits and costs. The proposed rule's scope is confined to establishing a framework for determinations that the Board is called upon by the HFCAA to make even absent a rulemaking. Additionally, neither the HFCAA nor the proposed rule gives the Board additional authority to take any action of legal consequence directly against a registered firm. Instead, the HFCAA contemplates that the Board would notify the Commission of its determinations, which may provide the predicate for other regulatory actions to be taken by the Commission if other conditions set forth in the HFCAA and the Commission's rules are met. This situation is in contrast to the direct impact of the

Board's statutory mandate to register, set professional standards for, inspect, investigate, and discipline registered firms. One commenter stated that economic benefits and costs arise from the HFCAA, which the PCAOB cannot change and must implement.

The Board's analysis of the potential benefits, costs, and unintended consequences of the proposed rule does not presuppose any determination that the Board may make under the proposed rule, because the Board would determine whether to make any future determinations based on the facts and circumstances at that time. The Board's analysis discusses the economic impacts of four central features of the proposed rule: (1) The Board's ability to make determinations as to a particular foreign jurisdiction; (2) limiting those jurisdiction-wide determinations to firms headquartered in the jurisdiction; (3) the Board's complementary ability to make determinations as to a particular registered firm; and (4) the Board's publication of its determinations on its website. The analysis is qualitative in nature because of a lack of information and data necessary to provide reasonable quantitative estimates. Overall, the Board expects that the benefits of the proposed rule will justify

<sup>118</sup> For purposes of Exhibit 1, a firm's jurisdiction is the jurisdiction where it is headquartered. The number of audit reports issued on the financial statements of issuers and the number of registered firms that issued those reports are based on issuer filings during the 12-month period ended June 30, 2021. The market capitalization of those issuers and the number of registered firms in each jurisdiction are as of June 30, 2021. Due to a lack of data on the number of shareholders, some audit reports included in Exhibit 1 may have been issued on the financial statements of entities with fewer than 300 shareholders. If a firm issued more than one audit report on financial statements filed by the same issuer during the 12-month period ended June 30, 2021, then only the most recent audit report is counted.

<sup>119</sup> See Audit Reports Issued by PCAOB-Registered Firms in Jurisdictions where Authorities Deny Access to Conduct Inspections, available at <https://pcaobus.org/oversight/ational/denied-access-to-inspections>. The information contained on this web page does not constitute a Board determination under the HFCAA. The Board has not yet made any determinations under the HFCAA.

any costs and unintended negative effects.

#### Benefits

The Board believes that the proposed rule would inform investors, registered firms, issuers, audit committees, foreign authorities, and the public at large as to how the Board will perform its functions under the HFCAA. The improved transparency and reduced regulatory uncertainty might help market participants make more efficient investment decisions and, hence, enhance capital formation. Furthermore, the proposed rule will promote consistency in the Board's processes regarding determinations. It will also assist the Commission in its consistent implementation of the HFCAA and achieving the statute's intended objectives. These are the primary benefits of the proposed rule. Several commenters agreed that a Board rule governing HFCAA determinations can improve regulatory transparency and consistency and reduce regulatory uncertainty.

The Board believes that the proposed rule's jurisdiction-wide determinations would yield additional benefits. In the Board's experience, when foreign authorities take a position that impairs the Board's oversight access, the position applies generally to all firms within the jurisdiction. Consequently, jurisdiction-wide determinations would provide an efficient, effective means of making Board determinations under the HFCAA.

Jurisdiction-wide determinations would be beneficial even when a foreign authority limits the Board's ability to inspect or investigate *certain types* of issuer audit engagements. Typically, the foreign authority's position applies to any firm in the jurisdiction that performs that type of engagement. If the Board were unable to make jurisdiction-wide determinations and instead were required to single out for determination only the specific audit firms handling those issuer engagements at a particular time, those issuers potentially could evade the consequences of the HFCAA by routinely changing audit firms in response to each successive firm-specific determination issued by the Board.<sup>120</sup> Beyond that, issuing a

jurisdiction-wide determination in such a scenario would help ensure that foreign authorities cannot, in essence, choose which firms within their jurisdiction the Board may inspect or investigate.

Limiting jurisdiction-wide determinations to firms headquartered in the jurisdiction would generate its own benefits. It would reduce the risk that a jurisdiction-wide determination sweeps too broadly by encompassing firms that merely have a physical presence or personnel in the jurisdiction but are headquartered elsewhere. Although a position taken by a foreign authority can naturally be understood to impact registered firms headquartered in the jurisdiction, its impact on firms that are headquartered elsewhere can turn on many factors, including the extent of the firm's presence in the jurisdiction and the nature and extent of the audit work it performs there. With that in mind, the proposed rule provides that the Board could choose to make individualized determinations with respect to firms that are headquartered elsewhere but have an office in such a jurisdiction.

Determinations as to a particular registered firm would complement the Board's jurisdiction-wide determinations by providing an additional option when the Board concludes that an across-the-board jurisdiction-wide determination is not appropriate. Such a provision recognizes that although the Board generally expects to make jurisdiction-wide determinations, it cannot anticipate every scenario it might encounter in the future. If a position taken by a foreign authority applies solely to one firm, which is expected to happen infrequently, the Board's ability to make a determination as to that firm would be a critical tool for fulfilling the HFCAA's objectives. Additionally, by providing an avenue for the Board to make determinations as to registered firms that are headquartered in a cooperating jurisdiction but have an office in a noncooperating jurisdiction, this provision would help ensure that the Board's flexibility under the proposed rule matches its mandate under the HFCAA.

The Board has also considered the potential benefits of making Board

determinations public on its website. Such publication would inform investors, registered firms, issuers, audit committees, foreign authorities, and the public regarding Board determinations, thus promoting transparency and reducing regulatory uncertainty. Market participants may benefit from being informed of Board determinations promptly, rather than waiting for the Commission's identification of covered issuers.

#### Costs and Unintended Consequences

The Board has also considered the potential costs and unintended consequences of the proposed rule. The Board expects any such costs and consequences to be limited, as the proposed rule merely establishes a framework for the Board to perform the responsibilities imposed upon it by the HFCAA.

The Board has evaluated the potential costs and unintended consequences of making jurisdiction-wide determinations. As explained in Section C above, such determinations treat all registered firms headquartered in the jurisdiction alike when the positions taken by authorities in the jurisdiction apply equally to any firm performing the same audit work for issuers, whether or not a particular registered firm happens to be doing such work when the Board makes a determination. To mitigate any perceived overinclusiveness or underinclusiveness of a jurisdiction-wide determination, the proposed rule limits those determinations to registered firms headquartered in the jurisdiction, while also permitting the Board, when appropriate, to supplement a jurisdiction-wide determination with a determination as to a particular firm that has an office in the jurisdiction but is not headquartered there.<sup>121</sup> This approach, in the Board's view, would be unlikely to impose incremental additional costs or lead to unintended consequences relative to the baseline, which consists of, among other things, the historical practice of identifying publicly the jurisdictions where there are unresolved obstacles to Board inspections and investigations.

The Board does not expect that the second central feature of the proposed rule—limiting jurisdiction-wide determinations to firms headquartered in the jurisdiction—would lead to

<sup>120</sup> If the Board were to make only firm-by-firm determinations based on each firm's then-current client portfolio, the Board might need to establish a process requiring all registered firms to report auditor changes to the Board in real time so that the Board could monitor such changes and promptly make new determinations in response. Presently, the Board's rules require firms to report their issuer clients to the Board only after the firm's audit report on the issuer has been issued. See PCAOB Rule 3211(b), *Auditor Reporting of Certain Audit*

*Participants* (Form AP must be filed within 35 days after the audit report is first included in a filing with the Commission, except that Form AP must be filed within 10 days if the audit report is included in a registration statement under the Securities Act). One commenter noted that jurisdiction-wide determinations would appear to be more efficient for the PCAOB's operations than determinations as to particular registered firms.

<sup>121</sup> Additionally, the Board has general residual exemption authority, subject to Commission approval, under Section 106(c) of the Act, and such authority could be used to address any potential overinclusiveness of a jurisdiction-wide determination.

additional costs or unintended consequences.

Related to the third central feature of the proposed rule—the Board’s ability to make determinations as to particular firms with an office in a foreign jurisdiction—one commenter encouraged the Board to consider the potential adverse impact on competition when assessing a potential future determination, and further encouraged the Board to provide equivalent treatment to similarly-situated firms. While any future determinations under the proposed rule as to particular registered firms may potentially have an impact on competition, such determinations, as noted in Section C above, are expected to be infrequent. Moreover, the magnitude of any impact would depend on many factors, such as the number of firms within the jurisdiction, the size of the firm as to which the determination is made, and how the foreign authority’s obstruction of the Board’s inspections or investigations has already affected competition in the jurisdiction.

Separately, the Board has evaluated the potential costs and unintended consequences of making its determinations public. The Board believes that the incremental costs of such publication will likely be minimal because similar information has historically been available on the Board’s website for approximately a decade.<sup>122</sup> Moreover, many issuers currently disclose in their annual reports the PCAOB’s inability to inspect their auditor, as the Commission recently observed.<sup>123</sup>

#### Alternatives Considered

As an alternative to a rulemaking, the Board considered issuing guidance related to its process or establishing a non-public process for making its determinations. The Board has determined, however, that a rule would reduce regulatory uncertainty for market participants by providing transparency and promoting consistency as to how the Board would perform its functions under the statute. Commenters generally agreed that a rule governing the Board’s determination process would promote

transparency and consistency and reduce regulatory uncertainty.

The Board also considered whether the proposed rule should be limited to determinations as to particular registered firms. Without jurisdiction-wide determinations, however, the Board would have to make determinations only as to particular firms under subparagraph (a)(2) of the proposed rule, potentially based on the present composition of each firm’s client portfolio. The Board believes that such an approach would incentivize an issuer whose audit engagement cannot be inspected or investigated by the Board to switch audit firms frequently, possibly frustrating the intent of the HFCAA and potentially necessitating a new process for real-time reporting of auditor changes to the Board so that Board determinations could be made or reassessed on a timely basis.

The Board also considered whether to extend its jurisdiction-wide determinations to all firms that have an office in the jurisdiction, rather than only those headquartered there. The Board elected not to do so, based on its oversight experience, because the impact of a position taken by a foreign authority on a firm headquartered elsewhere can vary based on the particulars of the firm’s presence, audit work, and issuer clients in the jurisdiction.

When prescribing the grounds upon which a determination may rest, the Board considered whether the Board’s commencement and subsequent inability to finish an inspection or investigation should be a prerequisite to a determination. The Board has not adopted that approach because the position taken by a foreign authority can frustrate the initiation of, or the ability to complete, an inspection or investigation. Moreover, commencing inspections or investigations in the face of such obstacles would be costly and fruitless, not only for the Board, but also for registered firms.

Lastly, although it can exercise exemption authority under Section 106(c) of the Act with the Commission’s approval,<sup>124</sup> the Board considered whether the proposed rule should include a procedure for the Board to grant exceptions from a jurisdiction-wide determination. The Board did not

include such a mechanism in the proposed rule for five principal reasons:

- An exception procedure would be inconsistent with the rationale for jurisdiction-wide determinations, namely, that the foreign authority has taken a position of such general scope and application that it obstructs the Board’s ability to complete inspections or investigations in that jurisdiction.

- To the extent that exception arguments would be based on the composition of a firm’s client portfolio at a moment in time, entertaining such arguments would require speculation as to whether the foreign authority would impede the Board’s ability to inspect or investigate those audits and would create a moving target as the firm gains and loses clients over time.

- Exceptions might increase the risk of a “shell game.” If a firm becomes subject to a Board determination because the Board cannot inspect certain types of issuer audit engagements it performed, those issuers might simply migrate to an excepted firm, triggering the need for the Board to monitor auditor changes constantly and then modify its determinations or revise its exceptions.

- An exception procedure might encourage foreign authorities to manipulate the determination process by cherry-picking certain firms that the PCAOB can inspect, thereby casting doubt on the justification for the Board’s jurisdiction-wide determination.

- Allowing firms to seek exceptions could effectively transform the Board’s jurisdiction-wide approach to a firm-by-firm approach that consumes substantial Board resources and fails to protect investors.

One commenter indicated that the Board’s existing exemption authority is adequate and expressed concern that granting exceptions could transform the Board’s jurisdiction-wide approach into a firm-by-firm approach that consumes substantial resources and fails to protect investors. The Board agrees with this commenter and has not created a procedure for granting exceptions from a jurisdiction-wide determination.

### III. Date of Effectiveness of the Proposed Rule and Timing for Commission Action

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Board consents, the Commission will:

<sup>122</sup> See, e.g., Audit Reports Issued by PCAOB-Registered Firms in Jurisdictions where Authorities Deny Access to Conduct Inspections, available at <https://pcaobus.org/over/international/denied-access-to-inspections>.

<sup>123</sup> See SEC Exchange Act Release No. 91364, at 26 (noting “a highly similar type and pattern of disclosure regarding the PCAOB’s inability to inspect those firms included in the majority of the potential Commission-Identified Issuers’ Item 3 (for Form 20-F filers) and Item 1A (for Form 10-K filers) discussion of risk factors”).

<sup>124</sup> See Section 106(c) of the Act (“[T]he Board, subject to the approval of the Commission, may, by rule, regulation, or order, and as [the Board] determines necessary or appropriate in the public interest or for the protection of investors, either unconditionally or upon specified terms and conditions exempt any foreign public accounting firm, or any class of such firms, from any provision of this Act or the rules of the Board . . . issued under this Act.”).

(A) By order approve or disapprove such proposed rule; or

(B) institute proceedings to determine whether the proposed rule should be disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule is consistent with the requirements of Title I of the Act. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission's internet comment form (<http://www.sec.gov/rules/pcaob.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. PCAOB-2021-01 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Vanessa Countryman, Secretary, U.S. Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090.

All submissions should refer to File No. PCAOB-2021-01. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's website (<http://www.sec.gov/rules/pcaob.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule that are filed with the Commission, and all written communications relating to the proposed rule between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549-1090, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filings will also be available for inspection and copying at the principal office of the PCAOB. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. All submissions should refer to File No. PCAOB-2021-01 and should be submitted on or before October 19, 2021.

For the Commission, by the Office of the Chief Accountant, by delegated authority.<sup>125</sup>

**Vanessa A. Countryman,**  
Secretary.

[FR Doc. 2021-21056 Filed 9-23-21; 4:15 pm]

BILLING CODE 8011-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-93102; File No. SR-OCC-2021-007]

### Self-Regulatory Organizations; the Options Clearing Corporation; Order Granting Approval of Proposed Rule Change Concerning the Options Clearing Corporation's Governance Arrangements

September 22, 2021.

#### I. Introduction

On July 30, 2021, the Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change SR-OCC-2021-007 ("Proposed Rule Change") pursuant to Section 19(b) of the Securities Exchange Act of 1934 ("Exchange Act")<sup>1</sup> and Rule 19b-4<sup>2</sup> thereunder to provide OCC's Board of Directors ("Board") with the discretion to elect either an Executive Chairman or a Non-Executive Chairman to preside over the Board, provide the Board and stockholders with the discretion to elect a Management Director, clarify the respective authority and responsibility of any Executive Chairman or Non-Executive Chairman, and make other clarifying, conforming, and administrative changes to OCC's rules.<sup>3</sup> The Proposed Rule Change was published for public comment in the **Federal Register** on August 11, 2021.<sup>4</sup> The Commission has received no comments regarding the Proposed Rule Change. This order approves the Proposed Rule Change.

#### II. Background<sup>5</sup>

Article III, Section I of OCC's By-Laws currently requires that the Board be composed of nine Member Directors,<sup>6</sup>

five Exchange Directors,<sup>7</sup> five Public Directors,<sup>8</sup> and an Executive Chairman (who also serves as a Management Director<sup>9</sup>). OCC's Executive Chairman is responsible for managing the Board while also being involved with the "day-to-day" management decisions of OCC. By contrast, a "Non-Executive Chairman" is typically not an employee of the company and focuses solely on leading and supporting its board of directors.

As described in more detail below, OCC proposes to revise its governing documents, including its By-Laws, Rules, Board of Directors Charter and Corporate Governance Principles ("Board Charter"), Audit Committee Charter, Compensation and Performance Committee Charter, Governance and Nominating Committee Charter, Risk Committee Charter, Technology Committee Charter (such committee charters collectively being the "Board Committee Charters"), and Amended and Restated Stockholders Agreement ("Stockholders Agreement"), to give the Board discretion to elect either an Executive or Non-Executive Chairman to preside over the Board. The Proposed Rule Change would also provide the Board and stockholders with discretion to elect Management Directors from OCC's management, which would be necessary if OCC does not have an Executive Chairman. OCC notes that the Proposed Rule Change would provide clarity around the authority and responsibilities of an Executive Chairman versus a Non-Executive Chairman.<sup>10</sup> OCC also proposes to make additional clarifying, conforming, and administrative changes to the documents listed above. OCC believes that the Proposed Rule Change would provide appropriate flexibility to the Board to evaluate OCC's governance arrangements, including whether OCC should have an Executive or Non-

to assure that (i) not all Member Directors are representatives of the largest Clearing Member organizations based on the prior year's volume, and (ii) the mix of Member Directors includes representatives of Clearing Member organizations that are primarily engaged in agency trading on behalf of retail customers or individual investors. See Article III, Section 5 of the OCC By-Laws.

<sup>7</sup> Exchange Directors represent the equity exchanges that are holders of Class B Common Stock of the OCC. Exchange Directors need not be Clearing Members or be associated with a Clearing Member organization. See Article III, Section 6 of the OCC By-Laws.

<sup>8</sup> Public Directors are independent directors who are not affiliated with any national securities exchange or national securities association or with any broker or dealer. See Article III, Section 6A of the OCC By-Laws.

<sup>9</sup> Management Directors also serve as employees of OCC. See Article III, Section 7 of the OCC By-Laws.

<sup>10</sup> See Notice of Filing *supra* note 4, 86 FR 44106.

<sup>125</sup> 17 CFR 200.30-11(b)(1) and (3).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Notice of Filing *infra* note 4, 86 FR 44105.

<sup>4</sup> Securities Exchange Act Release No. 92584 (Aug. 5, 2021), 86 FR 44105 (Aug. 11, 2021) (File No. SR-OCC-2021-007) ("Notice of Filing").

<sup>5</sup> Capitalized terms used but not defined herein have the meanings specified in OCC's Rules and By-Laws, available at <https://www.theocc.com/about/publications/bylaws.jsp>.

<sup>6</sup> Member Directors include Clearing Members or representatives of a Clearing Member. OCC endeavors to achieve balanced representation among Clearing Members on the Board of Directors