CENTER FOR CAPITAL MARKETS COMPETITIVENESS

TOM QUAADMAN
SENIOR VICE PRESIDENT

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December 7, 2015

Mr. Russ Golden
Chairman
Financial Accounting Standards Board
301 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-05116

Re: Proposed Amendments to Statement of Financial Accounting Concepts No. 8, *Conceptual Framework for Financial Reporting Chapter 3: Qualitative Characteristics of Useful Financial Information* (File Reference No. 2015-300)

Dear Chairman Golden:

The U.S. Chamber of Commerce (the "Chamber") created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy.[1] To achieve these goals, the CCMC has supported the development of robust financial reporting systems and encouraged efforts to improve standards and reduce complexity. The CCMC appreciates the opportunity to comment on the Financial Accounting Standards Board ("FASB") Exposure Draft on Statement of Financial Accounting Concepts No. 8—*Conceptual Framework for Financial Reporting, Chapter 3: Qualitative Characteristics of Useful Financial Information* ("the Proposal").

The Chamber strongly supports the Proposal and applauds the proactive leadership of FASB in defining materiality and resolving inconsistency between the well-established legal concept of materiality under the federal securities laws and the current usage of materiality as issued by FASB and the International Accounting Standards Board ("IASB"). Approval of the Proposal will lessen financial reporting complexity and ensure disclosure effectiveness by providing investors with decision

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[1] The Chamber is the world's largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information.

useful information and facilitating capital formation in a way that helps businesses and their investors. We have urged both the Securities and Exchange Commission ("SEC") and the Public Company Accounting Oversight Board ("PCAOB") to align definitions of materiality for financial reporting to reflect the legal concept of materiality under the federal securities laws so that each entity is using a common definition of materiality and creating a level playing field for regulators and marketplace stakeholders. This is a necessary cornerstone for capital markets that best serve the interests of investors and issuers.

Discussion

On October 9, 2013, the CCMC sent a letter to SEC Chair Mary Jo White, FASB Chair Russ Golden and PCAOB Chair James Doty outlining proposals for modernizing financial reporting policies.[2] Among the suggestions was a common definition of materiality amongst the regulator and standard setters. This is a necessary step forward to reducing complexity and confusion by placing accounting, auditing and SEC disclosures, as well as regulatory oversight on the same plane. Additionally, many stakeholders have complained about disclosure overload and voluminous disclosures that fail to provide decision useful information. The Proposal would address that concern, too.

In the eight decades since the securities laws were enacted, public company disclosure requirements have increasingly expanded and become more complex, as evidenced by the voluminous SEC reports public companies are now required to file.[3] This expansion and increased complexity of disclosure has contributed to the phenomenon of "disclosure overload," whereby investors are so inundated with information it becomes difficult for them to identify and digest the most salient information they need to make informed voting and investment decisions. Retail

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[2] The October 9, 2013 CCMC financial reporting modernization letter is attached hereto and we request that it be made part of the record along with this comment letter.

[3] For example, a 2012 report by Ernst & Young estimated that the average number of pages in annual reports devoted to footnotes and Management's Discussion and Analysis ("MD&A") has quadrupled over the last 20 years. Should this trend continue, companies would be devoting roughly 500 pages to MD&A by the year 2032. The Ernst & Young report can be found at: http://www.ey.com/Publication/vwLUAssets/ToThePoint_BB2367_DisclosureOverload_21June2012/$FILE/TothePoint_BB2367_DisclosureOverload_21June2012.pdf

investors are particularly vulnerable, as they often do not have the resources to help them make sense of the detailed SEC filings of the companies they invest in or might want to invest in. In fact, we believe the disclosure overload phenomenon is the leading contributor to why retail shareholder participation has dropped to levels as low as five percent at some annual shareholder meetings. In a very real way, disclosure overload has led to the disenfranchisement of retail shareholders at many public companies. Additionally, in a recent survey, only 38% of investors surveyed said they use audited financial statements as essential to the investment decision-making process.[4]

Retail shareholders aren't alone. A recent study by Professor David Larcker of Stanford University found that 55% of institutional investors surveyed felt the typical public company proxy statement is too long and 48% believe the typical proxy statement is too difficult to read and understand.[5]

The CCMC has long believed that the lodestar for SEC disclosure should be whether an incremental piece of information satisfies the traditional test of materiality set forth by the Supreme Court in the seminal case of TSC Industries Inc. v. Northway Inc.[6] There, Justice Thurgood Marshall, writing for the Court, explained "[M]anagement's fear of exposing itself to substantial liability may cause it simply to bury the shareholders in an avalanche of trivial information—a result that is hardly conducive to informed decision-making."[7] Marshall was concerned about disclosure overload harming investors and therefore set a more demanding test of materiality than some had urged. A fact is material, the Court held, if "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote."[8]

The Proposal would amend Chapter 3 of FASB Statement of Financial Accounting Concepts ("Concepts Statement") No. 8 to add the following statement:

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[4] *See* Center for Audit Quality Ninth Annual Main Street Investor Survey, September 2015, page 20.
[5] The investors surveyed had a total of $17 trillion under management. The study can be found at: http://www.gsb.stanford.edu/faculty-research/publications/2015-investor-survey-deconstructing-proxy-statements-what-matters.
[6] 426 U.S. 438 (1976).
[7] Id. at 448-49.
[8] Id. at 449.

> *Materiality is a legal concept. In the United States, a legal concept may be established or changed through legislative, executive, or judicial action. The Board observes but does not promulgate definitions of materiality. Currently, the Board observes that the U.S. Supreme Court's definition of materiality, in the context of the antifraud provisions of the U.S. securities laws, generally states that information is material if there is a substantial likelihood that the omitted or misstated item would have been viewed by a reasonable resource provider as having significantly altered the total mix of information.*[9]

The CCMC applauds FASB for taking this step to resolve the inconsistency between the legal concept of materiality in the United States and the current definition of materiality in Chapter 3 of Concepts Statement No. 8,[10] which was issued in 2010 as part of the convergence efforts of FASB and the IASB).[11] The CCMC has long encouraged FASB to address this issue,[12] as it is appropriate for the standard of materiality under the federal securities laws to control.

We recognize that Concepts Statements are not authoritative under the FASB Accounting Standards Codification ("ASC" or "Codification"). Nonetheless, the current inconsistency in definitions creates confusion and could increase litigation risks for companies and auditors alike, raising the very kind of concern that troubled the Supreme Court in *TSC Industries*—namely, disclosure overload that ultimately disadvantages investors.

Moreover, not only does the extant definition of materiality in Concepts Statement No. 8 differ from that based on longstanding jurisprudence interpreting the federal securities laws, but it also differs from guidance contained in FASB's

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[9] *See* page 3 of the Proposal.

[10] Concepts Statement No. 8 currently defines materiality as follows: "Information is material if omitting it or misstating it *could* influence decisions that users make on the basis of the financial information of a specific reporting entity" (emphasis added) (paragraph QC11, Chapter 3). It is important to note that in *TSC Industries* the Supreme Court rejected a threshold for determining materiality that is similarly low to *could*. In particular, the Court rejected the view that information is material if a reasonable investor *might* find it to be important. *TSC Industries*, 426 U.S. at 445-49.

[11] The CCMC has also encouraged IASB to adopt FASB's approach and recognize that materiality is a legal concept and defined by the jurisdiction in which International Financial Reporting Standards ("IFRS") are applied. *See* November 25, 2015 CCMC letter to the Honorable Hans Hoogervorst on the *Conceptual Framework for Financial Reporting*.

[12] For example, see the October 9, 2013 CCMC letter to the Honorable Mary Jo White on the modernization of financial reporting policies; the November 19, 2012 CCMC letter to FASB Chairman Russ Golden on the *Disclosure Framework* (File Reference 2012-220); and the July 14, 2014 CCMC letter to FASB Chairman Russ Golden on *Statement of Financial Accounting Concepts Chapter 8: Notes to Financial Statements* (File Reference No. 2014-200).

Codification itself. For example, ASC 250 includes Staff Guidance from the SEC for reference by public companies. ASC 250, likewise, incorporates a definition of materiality based on the Supreme Court decision—namely, that "a fact is material if there is a substantial likelihood that the…fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[13]

Further, the existing definition of materiality in Concepts Statement No. 8 also differs from that in the auditing standards of the PCAOB. For example, PCAOB Auditing Standard No. 11 states:

> *In interpreting the federal securities laws, the Supreme Court of the United Stated has held that a fact is material if there is 'a substantial likelihood that the…fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available.' As the Supreme Court has noted, determinations of materiality require 'delicate assessments' of the inferences a 'reasonable shareholder' would draw from a given set of facts and the significance of those inferences to him.…*

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It is essential that guidance on materiality by FASB, the SEC, and the PCAOB be aligned to conform to the well-established legal concept of materiality that the Supreme Court has established under the federal securities laws. We believe that this is important for investors to make informed decisions, for businesses to raise capital efficiently and for regulators to effectively oversee the capital markets. We commend FASB for its leadership in moving this important project forward. We stand ready to discuss any of the issues here with you further.

Sincerely,

Tom Quaadman

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[13] See FASB ASC 250-10-S99-1.

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TOM QUAADMAN
VICE PRESIDENT

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October 9, 2013

The Honorable Mary Jo White
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chair White:

The U.S. Chamber of Commerce (the "Chamber") is the world's largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy. To achieve these goals, the CCMC has supported the development of robust financial reporting systems and strong internal controls to promote efficient capital markets and capital formation.

We have read with interest recent reports that the Securities and Exchange Commission ("SEC") will step up its enforcement efforts, particularly focusing on potential accounting fraud and financial disclosure irregularities. The CCMC applauds the efforts of SEC to drive bad actors from the market place and create a level playing field for participants who operate in good faith and abide by the law. As SEC uses accounting fraud and financial reporting irregularities as a means to achieve this goal, we also believe that it is incumbent for SEC to modernize financial reporting policies to facilitate the release of relevant disclosures, reduce complexity, and achieve more efficient capital formation and competition. Accordingly, we would also respectfully request an update on the status of SEC's implementation of the recommendations of the Advisory Committee on Improvements to Financial Reporting ("CIFiR").

Modernization of financial reporting policies is well overdue.

In the wake of the Enron and WorldCom scandals and the subsequent passage of the Sarbanes-Oxley Act ("SOX"), financial reporting has undergone significant changes and transitions. Policy makers realized that financial reporting must keep pace with those changes. Consequently, then SEC Chairman Chris Cox formed CIFiR, which released its report and recommendations to improve financial reporting in August 2008. Unfortunately, the demands of the financial crisis diverted the time and attention of the agency from its ongoing agenda of

modernizing financial reporting. We believe that the implementation of these recommendations remains an urgent item on SEC's agenda.

Adding to the urgency of these recommendations is the pace of change in financial reporting that has taken place since the financial crisis. Among the many new legislative, regulatory, and standard-setting requirements that have influenced financial reporting in the last few years is the Jumpstart Our Business Startups Act ("JOBS Act"). This law exempts emerging growth companies ("EGCs") from new rules of the Public Company Accounting Oversight Board ("PCAOB"), unless SEC determines that those rules are necessary and in the public interest[1], and allows EGCs to comply with any new or revised Financial Accounting Standards Board ("FASB") standards in the same timeframe as companies that are not issuers. Similarly, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") has profoundly impacted and exacerbated many of the issues identified in the CIFiR report.

For these reasons, it is important for SEC to adopt a comprehensive approach to modernizing financial reporting policies that includes, in addition to stepped-up enforcement, increased communication and cooperation among regulators, standard setters and stakeholders. This will reinforce SEC's efforts to drive bad actors out of the marketplace, by eliminating the complexity and ambiguity on which they thrive. In fact, the CIFiR report found that financial reporting complexity is a key driver in the disconnection between current financial reporting and the information necessary to make sound investment decisions. Since keeping a clear focus on SEC's mission to ensure that investors receive relevant decision-useful information and to promote capital formation will maximize the agency's chances of success in stamping out accounting fraud and financial disclosure irregularities, we view this as a win-win for SEC and its stakeholders.

Listed below are some of the issues and suggested solutions to improve financial reporting.

Issues and Proposed Solutions

Issue 1: Provide Investors with Information Needed for Sound Decision Making

Problem: Inconsistent definitions of materiality.

Solution: The SEC should supplement existing guidance and coordinate in such a way to ensure that SEC, FASB and PCAOB use a common definition of materiality.

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[1] *See* letter from the Chamber to the SEC (October 5, 2012) that Section 104 of the JOBS Act requires an analysis and finding that new PCAOB standards and revisions must promote efficiency, competition and capital formation in order to apply to EGCs.

Background: FASB has defined materiality for U.S. Generally Accepted Accounting Principles ("U.S. GAAP") differently than the securities laws, while the PCAOB is using the definition from the federal securities laws.

PCAOB Auditing Standard No. 11 states in part:

> *In interpreting the federal securities laws, the Supreme Court of the United States has held that a fact is material if there is 'a substantial likelihood that the ... fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available.' As the Supreme Court has noted, determinations of materiality require 'delicate assessments' of the inferences a 'reasonable shareholder' would draw from a given set of facts and the significance of those inferences to him ...*

FASB Concept Statement No. 8 uses the following definition: "Information is material if omitting it or misstating it *could* influence decisions that users make on the basis of the financial information of a specific reporting entity."[2]

Additionally, FASB's Invitation to Comment on Disclosure Framework (File Reference 2012-220), states that reporting entities would assess the relevance of each disclosure using the basic criterion that "information should be disclosed if it has the potential to make a difference in users' decisions about providing resources to the reporting entity."[3] [4]

CIFiR recommended that the FASB or SEC, as appropriate, should supplement existing guidance to reinforce that:

> *Those who evaluate the materiality of an error should make the decision based upon the perspective of a reasonable investor; and, materiality should be judged based* on *how an error affects the total mix of information available to a reasonable investor, including through a consideration of qualitative and quantitative factors*.[5]

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[2] Par. QC11, Chapter 3

[3] FASB Invitation to Comment on Disclosure Framework, paragraph 4.5 (page 45).

[4] For additional insights on the issues, see "What is Materiality? SEC & PCAOB v. FASB & ASB" by Samuel P. Gunther in *Bloomberg BNA* (May 7, 2012).

[5] Recommendation 3.1, page 80, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

It should also be noted that the International Integrated Reporting Council ("IIRC") and the Sustainability Accounting Standards Board ("SASB") are creating their own concepts of materiality in attempting to develop voluntary standards of non-financial reporting and disclosure – with the SASB's disclosures intended to be included within Management Discussion and Analysis ("MD&A") in Form 10-K and 10-Q filings with SEC. The Chamber has written to both organizations expressing concerns that the development of these standards needs to be done with SEC and that any work in this area must conform to the definitions, usage, and enforcement of materiality as defined in the Securities Acts and their progeny.[6] Similarly, in testimony before the U.S. Senate Subcommittee on Securities, Insurance, and Investment the Chamber stated:

> *The SEC, FASB, and PCAOB should develop standards of materiality for investors, as well as the scope of outreach to the investor community. This will provide perspective on various accounting and auditing issues such as the need for restatements on the one end, while framing the picture for input on the front end of standard setting.*[7]

<u>Problem</u>: Information overload from multiple overlapping and sometimes contradictory reporting and disclosure requirements and standards.

<u>Solution:</u> Develop a Disclosure Framework.

<u>Background:</u> CIFiR recommended that SEC and FASB work together to develop a disclosure framework to, among other things:

> *Integrate existing SEC and FASB disclosure requirements into a cohesive whole to ensure meaningful communication and logical presentation of disclosures, based on consistent objectives and principles. This would eliminate redundancies and provide a single source of disclosure guidance across all financial reporting standards.*[8]

A disclosure framework would also address issues of placement of information within audited U.S. GAAP financial statements versus MD&A which is unaudited, has safe harbors and provides forward looking information.[9]

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[6] *See* letters from the Chamber to IIRC (July 15, 2013) and SASB (July 26, 2013).

[7] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance and Investment (April 6, 2011).

[8] Recommendation 1.2, page 8, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

[9] FASB currently has a disclosure framework project in progress and the SEC Chief Accountant announced in February, 2013 that a SEC Staff Paper on disclosure is expected to be released with roundtables planned to follow.

<u>Problem:</u> The accounting standards setters continue down the path of including the recognition, measurement, and disclosure of more fair values and accounting estimates that require judgment and, therefore, investors and others cannot expect there to be a single "right answer" in accounting and auditing matters.

<u>Solution:</u> Issue a policy statement articulating how SEC evaluates the reasonableness of accounting judgments.

<u>Background:</u> CIFiR recommended that:

> *The SEC issue a statement of policy articulating how it evaluates the reasonableness of accounting judgments and include factors that it considers when making this evaluation. The statement of policy applicable to accounting-related judgments should address the choice and application of accounting principles, as well as estimates and evidence related to the application of an accounting principle. … We believe that it would be useful if the SEC also set forth in the statement of policy factors that it looks to when evaluating the reasonableness of preparers' accounting judgments.*[10]

<u>Solution</u>: The PCAOB should issue a policy statement on how it evaluates the reasonableness of audit judgments.[11]

<u>Background:</u> CIFiR recommended that:

> *[T]he PCAOB develop and articulate guidance related to how the PCAOB, including its inspections and enforcement divisions, would evaluate the reasonableness of judgments made based on PCAOB auditing standards. The PCAOB's statement of policy should acknowledge that the PCAOB would look to SEC's statement of policy to the extent that the PCAOB would be evaluating the appropriateness of accounting judgments as part of an auditor's compliance with PCAOB auditing standards.*[12]

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[10] Recommendation 3.5, pages 13-14, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

[11] *See* various CCMC comment letters including to the PCAOB on Request for Public Comment on Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards and Notice of Roundtable (PCAOB Release No. 2011-003, June 21, 2011, Rulemaking Docket Matter No. 34).

[12] Recommendation 3.5, page 14, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

Solution: The SEC work with the FASB and PCAOB to consider the auditability of GAAP when developing accounting standards and disclosure requirements.

Background: Again in testimony before the U.S. Senate Subcommittee on Securities, Insurance, and Investment the Chamber stated:

> *A formal, ongoing, and transparent dialogue should be created to consider the auditability of accounting standards. This would allow for the auditing of accounting standards to work in conjunction with standard development. It would also provide for the identification and resolution of issues that arise in practice. A similar process should be created to ensure that regulators have an understanding of standards and that different entities are not working at cross purposes. The era of "not my problem" needs to end.*[13]

Solution: Conduct formal pre and post-implementation reviews.

Background: CIFiR recommended that the Financial Accounting Foundation ("FAF"), FASB, and other participants in the financial reporting system:

> *Enhance the consistency and transparency of key aspects of FASB's field work, including cost-benefit analyses, field visits, and field tests.*
>
> *Formalize post-adoption reviews of each significant new standard to address interpretive questions and reduce the diversity of practice in applying the standard, if needed.*
>
> *Formalize periodic assessments of existing accounting and related disclosure standards to keep them current.* [14]

The Chamber reinforced this notion by stating that standards should be field tested and put through a rigorous process to identify unintended consequences before implementation and after implementation.[15]

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[13] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance and Investment (April 6, 2011).

[14] Included in recommendation 2.3, page 11, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

[15] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance, and Investment (April 6, 2011).

The Chamber appreciates that the FAF and FASB are moving in the direction of this recommendation and we suggest that the PCAOB should do likewise and that SEC should ensure that the FASB and PCAOB are coordinated in these efforts.

Issue 2: Increase Communication and Coordination amongst Regulator and Standard Setters

Problem: Lack of transparent communication and coordination among regulators, standard setters and market participants.

Solution: Establish a Financial Reporting Forum ("FRF").

Background: CIFiR recommended the creation of a FRF, made up of the SEC, FASB, PCAOB, financial regulators, investors (broadly defined), and businesses, with a mission to identify and propose solutions to problems before they reach the crisis stage. A FRF will also provide a mechanism to allow for appropriate coordination amongst regulators and input from investors and businesses.[16] It should also be noted that in the 111th Congress, the House of Representatives passed a version of H.R. 4173, the precursor bill of the Dodd-Frank Act, which contained an amendment by Rep. Gary Miller to create an FRF.

Problem: Potential expectation gap created by the PCAOB's recent definition of an audit failure.

Solution: Through the exercise of SEC's oversight authority over the PCAOB reestablish the long-standing definition of an audit failure.

Background: Several years ago and without explanation, the PCAOB began describing Part I deficiencies as audit failures in inspection reports for annually inspected firms (although the PCAOB does not use these terms in inspection reports for tri-annually inspected firms). This change in definition contradicted the long-standing and widely used definition of an audit failure as used by the Government Accountability Office ("GAO"). GAO defined audit failures as:

> *[A]udits for which audited financial statements filed with the SEC contained material misstatements whether due to errors or fraud, and reasonable third parties with knowledge of the relevant facts and circumstances would have concluded that the audit was not conducted in accordance with generally accepted auditing standards, and, therefore, the auditor failed to appropriately detect and/or deal with known material misstatements by (1) ensuring that*

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[16] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance, and Investment (April 6, 2011).

> *appropriate adjustments, related disclosures, and other changes were made to the financial statements to prevent them from being materially misstated, (2) modifying the auditor's opinion on the financial statements if appropriate adjustments and other changes were not made, or (3) if warranted, resigning as the public company's auditor of record and reporting the reason for the resignation to the SEC.*[17]

In other words, for example, differences of opinion in the exercise of judgment on audit procedures or other audit deficiencies – which do not occur in conjunction with any material misstatement of the financial statements – could not be considered an audit failure.

You will also find with this letter, as an attachment, a letter sent by the Chamber to PCAOB Chairman James Doty that contains a more robust discussion of our concerns on the failure to properly define audit failure, the communication, and portrayal of inspections findings and how it may undermine public confidence in financial reporting.

Issue 3: Reduce Fraudulent Financial Reporting

Problem: Lack of a comprehensive and holistic approach to understanding fraudulent financial reporting, diagnosing its root causes and detecting fraud through the application of useful and appropriate methodologies and technologies.

Solution: Establish a Fraud Center.

Background: The Advisory Committee on the Audit Profession ("ACAP") recommended:

> *SEC and Congress, as appropriate, provide for the creation by the PCAOB of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.*[18]

Financial reporting frauds undermine investor confidence in the capital markets. In October 2010, the Center for Audit Quality (CAQ) formally joined forces to form an Anti-Fraud Collaboration with Financial Executives International, The Institute of Internal Auditors, and the

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[17] *See* GAO 04-217 Public Accounting Firms Required Study on the Potential Effects of Mandatory Audit Firm Rotation (2003) page 6.
[18] ACAP Final Report (October 6, 2008), page VII:1

National Association of Corporate Directors to develop thought leadership, awareness programs, educational opportunities, and other related resources specifically targeted to the unique roles and responsibilities of the primary participants in the financial reporting supply chain. The projects and activities under this Anti-Fraud Collaboration are designed to enhance awareness and understanding of factors that contribute to financial reporting fraud, as well as strengthen the abilities of all applicable parties' efforts to deter and/or detect financial reporting fraud. These types of private sector initiatives can lead to long term progress in combating threats to investor confidence in the U.S. capital markets.

Since fraud can never be completely prevented, efforts to combat fraud must be continuous. All key participants in the financial reporting supply chain – preparers, audit committee members, auditors, *and regulators* – have important roles to play with regard to deterring and detecting financial reporting fraud. We believe the PCAOB can and should do more with the information it has accumulated through its various programs to identify trends, best practices, and specific actions that could be shared with auditors and preparers to assist in the deterrence or detection of financial statement fraud.

Issue 4: Increase Transparency and Accountability of FASB and PCAOB

Problem: Neither the FASB nor the PCAOB are formally subject to the traditional regulatory provisions for accountability and transparency.

Solution: Both the FASB and PCAOB and their attendant advisory groups should abide by the same rules of procedures as required of regulatory agencies by the Administrative Procedures Act and Federal Advisory Committee Act, including any advisory groups should be balanced in presentation and open in process.[19]

Solution: The PCAOB should form a Business Advisory Group to understand the role of companies as investors, their use of investments, and the potential impact of standard setting on businesses. The PCAOB should also establish an Audit Advisory Group to more substantively bring the expertise of practicing auditors to inform the PCAOB's activities and initiatives.[20]

Background: For example, a Business Advisory Group would provide the PCAOB another means of input and broader understanding of issues that need to be addressed in the development of standards and other means of resolving important issues related to audited

[19] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance and Investment (April 6, 2011).
[20] Ibid.

financial statements. This dialogue could help the PCAOB better appreciate business operations and the unintended consequences that may impact businesses through the development and implementation of accounting and auditing standards. The avoidance of adverse outcomes for businesses is critical to protect the investors who invest in them.[21]

Issue 5: Addressing the needs of Private Company financial statement users

Problem: Private company financial statement users have differing needs and find public company U.S. GAAP to be too complex and burdensome.

Solution: Preserve U.S. GAAP as the accounting language, while empowering the Private Company Council to address the needs of private company users.

Background: Any modernization of financial reporting policies requires that the differing needs of users of the financial statements be considered and addressed. In particular, privately held users do not require the same information as users those entities that are owned by the public. It is imperative that any changes made to standards do not have the unintended consequence of requiring privately held entities to follow standards which may provide information critically important to users of publically held entity financial statements but which is not relevant to their users. While CIFiR did not address these issues, following extensive study and research, the Blue Ribbon Panel on Standard Setting for Private Companies ("Blue Ribbon Panel") made several recommendations which eventually led to the creation of the Private Company Council under the auspices of the FAF. Additionally, Congress, in passing the JOBS Act, made the public policy decision that users of financial reports are not monolithic and different business structures (ie. public company, emerging growth companies) will dictate the needs of financial statement users. Accordingly, we believe the SEC, FRF, and FAF should closely monitor the activities of the PCC to ensure the needs of private company users are met and that the Congressional intent of the JOBS Act is fulfilled.

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This is not an exhaustive list of reforms or issues that should be addressed. Rather, we view this as a starting point of discussion and would respectfully request to meet with you to discuss these ideas and proposals in greater depth and detail. While we know and appreciate the workload of SEC, it is our belief that the many changes in financial reporting over the past decade require a response to prevent disharmony in financial reporting that can adversely impact the capital markets, businesses and the investors who provide them with the resources to grow and operate on a daily basis.

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[21] *See* CCMC letter to Martin F. Baumann (May 10, 2013).

Thank you for your consideration of these views, and we look forward to further discussion with you and SEC staff as well as an update on the implementation of the CIFiR recommendations.

Sincerely,

Tom Quaadman

cc: The Honorable Luis A. Aguilar, U.S. Securities and Exchange Commission
The Honorable Daniel Gallagher, U.S. Securities and Exchange Commission
The Honorable Kara Stein, U.S. Securities and Exchange Commission
The Honorable Michael Piwowar, U.S. Securities and Exchange Commission
Mr. Paul Beswick, U.S. Securities and Exchange Commission
Mr. Russell Golden, Financial Accounting Standards Board
Mr. James Doty, Public Company Accounting Oversight Board
The Honorable Tim Johnson, U.S. Senate
The Honorable Michael Crapo, U.S. Senate
The Honorable Jeb Hensarling, U.S. House of Representatives
The Honorable Maxine Waters, U.S. House of Representatives
The Honorable Scott Garrett, U.S. House of Representatives
The Honorable Carolyn Maloney, U.S. House of Representatives