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RULES ON INVESTIGATIONS ) PCAOB Release No. 2003-015  
AND ADJUDICATIONS ) September 29, 2003  
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) PCAOB Rulemaking  
) Docket Matter No. 005  
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**Summary:** After public comment, the Public Company Accounting Oversight Board ("Board" or "PCAOB") has adopted rules on investigations and adjudications. The rules would govern investigations and hearings in disciplinary proceedings, pursuant to Section 105 of the Sarbanes-Oxley Act ("Act"), and hearings on registration applications pursuant to Section 102 of the Act. The Board will submit these rules to the Securities and Exchange Commission ("Commission") for approval pursuant to Section 107 of the Act. The Board's rules will not take effect unless approved by the Commission.

**Board**

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\* \* \*

Section 105 of the Act grants the Board broad investigative and disciplinary authority over registered public accounting firms and persons associated with such firms. To implement this authority, Section 105(a) directs the Board to establish, by rule, fair procedures for the investigation and discipline of registered public accounting firms and associated persons of such firms. As directed by the Act, the Board has adopted rules relating to investigations and adjudications.

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The rules on investigations and adjudications consist of 64 rules (PCAOB Rules 5000 through 5501), plus certain definitions that would appear in Rule 1001 and a rule on time computation that would be Rule 1002. Appendices 1 and 2 to this release contain, respectively, the text of these rules and a section-by-section analysis of the rules. Section A of this release provides a general overview of the operation of the rules. Section B of this release describes the changes made to the rules in response to public comments.

A. Operation of the Rules on Investigations and Adjudications

Under the rules, the Board and its staff may conduct investigations concerning any acts or practices, or omissions to act, by registered public accounting firms and persons associated with such firms, or both, 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 issued under the Act, or professional standards. The Board's rules require registered public accounting firms and their associated persons to cooperate with Board investigations, including producing documents and providing testimony. The rules also permit the Board to seek information from other persons, including clients of registered firms.

When violations are detected, the Board will provide an opportunity for a hearing, and in appropriate cases, impose sanctions designed to deter a possible recurrence and to enhance the quality and reliability of future audits. The sanctions may be as severe as revoking a firm's registration or barring a person from participating in audits of public companies. Lesser sanctions include monetary penalties and requirements for remedial measures, such as training, new quality control procedures, and the appointment of an independent monitor.

The Board may also hold hearings on registration applications, pursuant to Section 102 of the Act. Under the Board's registration rules, if the Board is unable to determine that a public accounting firm has met the standard for approval of an application, the Board may provide the firm with a notice of a hearing, which the firm may elect to treat as a written notice of disapproval for purposes of making an appeal to the Commission under Section 107. If such a firm chooses instead to request a hearing, the Board would, in appropriate circumstances, afford the firm a hearing pursuant to the rules.

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With the exception of the changes discussed in Section B below, the rules adopted today are substantially similar to the rules proposed by the Board on July 28, 2003. The operation of those rules was summarized in greater detail in PCAOB Release No. 2003-012 (July 28, 2003).

- Special Issues Relating to Non-U.S. Firms

The nature and scope of the Board's oversight over non-U.S. accounting firms that audit the financial statements of U.S. public companies is the subject of an ongoing dialogue between the Board and its foreign counterparts. As the Board has previously stated, the Board is committed to accomplishing the oversight goals of the Act by coordinating in areas where there is a common programmatic interest without subjecting non-U.S. firms to unnecessary burdens. The adoption of these rules is not intended in any way to signal that the Board has already determined how its oversight should operate as to those firms. Before non-U.S. accounting firms are required to register with the Board, the Board intends to issue a release describing how it will carry out its investigative and disciplinary responsibilities with respect to such firms.

B. Public Comment Process and Board Responses

The Board proposed rules on investigations and adjudications, and released them for public comment, on July 28, 2003. The Board received 17 written comment letters.<sup>1/</sup> In response to these comments, the Board's final rules both clarify and modify certain aspects of the proposal. Most importantly, the changes include –

- Clarifying the Board's views of what privileges may be invoked in Board proceedings, including that the Board will not treat proper invocations of the Fifth Amendment privilege against self-incrimination as noncooperation;
- Reducing the reach of noncooperation sanctions in the context of testimony, by eliminating the possibility that omitting material information, can, by itself, be grounds for a noncooperation proceeding;

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<sup>1/</sup> The Board's responses to the comments are discussed in more detail in the section-by-section analysis in Appendix B. The comment letters are available on the Board's website – [www.pcaobus.org](http://www.pcaobus.org) – and will be attached to the Board's Form 19b-4, to be filed with the Commission.

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- Specifying that the Board staff bears the burden of proof by a preponderance of the evidence in a disciplinary proceeding;
- Clarifying that the Board will not withhold material exculpatory evidence from a respondent;
- Requiring that any exercise of the Board's authority to conduct an examination to verify information supplied in an investigation must be approved by the Director of the Board's Division of Enforcement and Investigations;
- Clarifying how a bar or suspension of an associated person affects the ways in which a firm may compensate that person;
- Clarifying in the rules that all staff in the Board's Division of Enforcement and Investigations will be excluded from participating in the adjudication of any disciplinary proceeding;
- Revising the definition of "hearing officer" to provide that neither a Board member nor interested staff may serve as a hearing officer;
- Expanding the scope of the Board's staff that is covered by restrictions on ex parte communications with the Board after a disciplinary proceeding is authorized;
- Providing that firms can produce copies of documents in response to a demand for the production of documents, unless the accounting board demand expressly requires originals to be produced;
- Providing that permission for an attorney to withdraw as counsel in a proceeding before the Board or a hearing officer will not be unreasonably withheld;
- Extending the time for witnesses to request changes to the transcript of their testimony;



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- Requiring Board staff to provide a "privilege log" for certain documents that the staff withholds from respondents based on a claim of privilege;
- Revising the procedures for appeals to the Board of actions taken by Board staff under delegated authority;
- Allowing state regulatory authorities to participate in a proceeding for purposes of requesting a stay of the proceeding; and
- Clarifying when a firm's registration may be suspended for failing to pay a money penalty.

\* \* \*

On the 29th day of September, in the year 2003, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour  
Acting Secretary

September 29, 2003

APPENDICES –

1. Rules Relating to Investigations and Adjudications
2. Section-by-Section Analysis of Rules Relating to Investigations and Adjudication

**Appendix 1 – Proposed Rules Relating to Investigations and Adjudications**

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## RULES OF THE BOARD

### SECTION 1. GENERAL PROVISIONS

#### **Rule 1000. [Reserved]**

#### **Rule 1001. Definitions of Terms Employed in Rules**

When used in the Rules, unless the context otherwise requires –

##### **(a)(ix) Accounting Board Demand**

The term "accounting board demand" means a command to produce documents and/or to appear at a certain time and place to give testimony.

##### **(a)(x) Accounting Board Request**

The term "accounting board request" means a request to produce documents and/or to appear at a certain time and place to give testimony.

##### **(b)(ii) Bar**

The term "bar" means a permanent disciplinary sanction prohibiting a person from being associated with a registered public accounting firm.

##### **(c)(ii) Counsel**

The term "counsel" means an attorney at law admitted to practice, and in good standing, before the Supreme Court of the United States or the highest court of any state.

##### **(d)(i) Disciplinary Proceeding**

The term "disciplinary proceeding" means a proceeding initiated by an order instituting proceedings, held for the purpose of determining whether or not a registered public accounting firm, or any person associated with a registered public accounting firm, has engaged in any act or practice, or omitted to act, in violation 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 issued under the Act, or professional standards; or has failed reasonably to supervise an associated person in connection with any such violation by that person; or has failed to cooperate with the Board in

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connection with an investigation; and whether to impose a sanction pursuant to Rule 5300.

**(d)(ii) Document**

The term "document" is synonymous in meaning and equal in scope to its usage in Federal Rule of Civil Procedure 34(a), including, without limitation, electronic or computerized data compilations. A draft or non-identical copy is a separate document within the meaning of this term. In no event shall the term "document" be construed to be limited to audit work papers.

**(h)(i) Hearing Officer**

The term "hearing officer" means a person, other than a Board member or staff of the interested division, duly authorized by the Board to preside at a hearing.

**(i)(iv) Interested Division**

The term "interested division" means a division or office of the Board assigned primary responsibility by the Board to participate in a particular proceeding.

**(o)(ii) Order Instituting Proceedings**

The term "order instituting proceedings" means an order issued by the Board commencing a disciplinary proceeding.

**(p)(iii) Party**

The term "party" means the interested division, any person named as a respondent in an order instituting proceedings or notice of a hearing, any applicant named in the caption of any order, or any person seeking Board review of a decision.

**(p)(iv) Person**

The term "person" means any natural person or any business, legal or governmental entity or association.

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**(r)(iii) Revocation**

The term "revocation" means a permanent disciplinary sanction terminating a firm's registration.

**(s)(iii) Secretary**

The term "Secretary" means the Secretary of the Board.

**(s)(iv) Suspension**

The term "suspension" means a temporary disciplinary sanction, which lapses by its own terms, prohibiting –

(1) a registered public accounting firm from preparing or issuing, or participating in the preparation or issuance of, any audit report with respect to any issuer; or

(2) a person from being associated with a registered public accounting firm.

**Rule 1002. Time Computation**

In computing any period of time prescribed in or allowed by these Rules or by order of the Board, the day of the act, event, or default from which the designated period of time begins to run shall not be included. The last day of the period so computed shall be included unless it is a Saturday, Sunday, or federal legal holiday, in which event the period runs until the end of the next day that is not a Saturday, Sunday, or federal legal holiday. Intermediate Saturdays, Sundays, and federal legal holidays shall be excluded from the computation when the period of time prescribed or allowed is seven days or less, not including any additional time allowed by rule or order for service by mail. If on the day a filing is to be made, weather or other conditions have caused the Secretary's office or other designated filing location to close, the filing deadline shall be extended to the end of the next day that is neither a Saturday, a Sunday, nor a federal legal holiday.

Note: The Secretary will maintain a list of federal legal holidays.

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## **SECTION 5. INVESTIGATIONS AND ADJUDICATIONS**

### **Rule 5000. General**

A registered public accounting firm, and any person associated with such a firm, shall comply with all Board orders to which the firm or person is subject.

### **Part 1 – Inquiries and Investigations**

#### **Rule 5100. Informal Inquiries**

##### **(a) Commencement of an Informal Inquiry**

The Director of Enforcement and Investigations may undertake an informal inquiry where it appears that, or to determine whether, an act or practice, or omission to act, by a registered public accounting firm, any associated person of that firm, or both, may violate –

- (1) any provision of the Act;
- (2) the Rules of the Board;
- (3) 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
- (4) professional standards.

##### **(b) Informal Inquiry Activities**

In an informal inquiry, the Director of Enforcement and Investigations may request documents, information or testimony from, or an interview with, any person.



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**Rule 5101. Commencement and Closure of Investigations**

**(a) Commencement of Investigations**

**(1) Order of Formal Investigation**

Upon the recommendation of the Director of Enforcement and Investigations or the Director of Registration and Inspections, or upon the Board's own initiative, or otherwise, the Board may issue an order of formal investigation when it appears that an act or practice, or omission to act, by a registered public accounting firm or any person associated with a registered public accounting firm 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 issued under the Act, or professional standards.

**(2) Designation of Staff**

In an order of formal investigation, the Board may designate members, or groups of members, of the Board's staff to issue accounting board demands to, and otherwise require or request cooperation of, any person pursuant to Section 105(b)(2) of the Act, and the Board's Rules thereunder, to the extent the information sought is relevant to the matters described in the Board's order of investigation.

**(b) Closure of Investigations**

Upon the recommendation of the Director of Enforcement and Investigations, or on its own initiative, the Board may issue an order terminating or suspending, for a specified period of time, a formal investigation.

**Rule 5102. Testimony of Registered Public Accounting Firms and Associated Persons in Investigations**

**(a) General**

The Board, and the staff of the Board designated in an order of formal investigation, may require the testimony of any registered public accounting firm or any

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person associated with a registered public accounting firm, with respect to any matter that the Board considers relevant or material to an investigation.

**(b) Accounting Board Demand for Testimony**

The Board, and the staff of the Board designated in an order of formal investigation, shall require testimony by serving an accounting board demand that –

(1) gives reasonable notice of the time and place for the taking of testimony;

(2) states the method or methods by which the testimony shall be recorded, which may be by sound or sound-and-visual, but shall include by stenographic means; and

(3) if the person to be examined is a registered public accounting firm, a description with reasonable particularity of the matters on which examination is requested.

**(c) Conduct of Examination**

**(1) Oath or Affirmation**

Before testifying, every witness shall be required to declare that the witness will testify truthfully, by oath or affirmation administered in a form calculated to awaken the witness's conscience and impress the witness's mind with the duty to do so.

**(2) General**

Examinations shall be conducted before a reporter designated by the Board's staff.

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**(3) Persons Permitted to be Present**

Persons permitted to be present at an examination pursuant to this Rule are limited to –

- (i) the person being examined and his or her counsel, subject to Rule 5109(b);
- (ii) any Board member or member of the staff of the Board;
- (iii) the reporter; and
- (iv) such other persons as the Board, or the staff of the Board designated in the order of formal investigation, determine are appropriate to permit to be present; provided, however, that in no event shall a person other than the witness who has been or is reasonably likely to be examined in the investigation be present.

**(4) Examinations of Registered Public Accounting Firms**

A registered public accounting firm subject to an accounting board demand shall designate one or more individuals who consent to testify on its behalf, and may set forth, for each individual designated, the matters on which the individual will testify. The individuals so designated shall testify as to matters known or reasonably available to the registered public accounting firm.

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**(d) Transcript**

A witness shall have 15 days, or such longer period as the Director of Enforcement and Investigations may allow, after being notified by the reporter that the transcript, or, where applicable, video or other recording, is available in which to review the transcript or other recording and, if there are changes in form or substance, to sign a statement reciting such changes and the reasons given by the witness for making them. The reporter shall make a certificate in writing to accompany the transcript, which shall indicate –

(1) that the witness was duly sworn by the officer and that the transcript is a true record of the testimony given by the witness; and

(2) whether the witness requested to review the transcript and, if so, that the reporter has appended any changes made by the witness during the period allowed.

**Rule 5103. Demands for Production of Audit Workpapers and Other Documents from Registered Public Accounting Firms and Associated Persons**

**(a) General**

The Board, and the staff of the Board designated in an order of formal investigation, may issue an accounting board demand for the production of audit work papers or any other document or information in the possession of a registered public accounting firm or any associated person thereof, wherever domiciled, that the Board or its staff considers relevant or material to the investigation.

**(b) Time and Manner of Production**

An accounting board demand shall set forth a reasonable time and place for production. Unless an accounting board demand expressly requires the production of original documents, copies of the requested documents may be produced. If the originals are not produced, they shall be maintained in a reasonably accessible manner, shall be readily available for inspection by the staff, and shall not be destroyed without the staff's consent. Unless an accounting board demand expressly requests or permits printed copies of electronic documents, documents that exist in electronic form shall be produced in that form.

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**Rule 5104. Examination of Books and Records in Aid of Investigations**

Upon demand and without regard to the Board's Rules under Section 104 of the Act, the Board, and, with the approval of the Director of Enforcement and Investigations, the staff of the Board designated in an order of formal investigation, may examine the books and records of any registered public accounting firm or associated person to verify the accuracy of any documents or information supplied in the course of an informal inquiry or formal investigation.

**Rule 5105. Requests for Testimony or Production of Documents from Persons Not Associated With Registered Public Accounting Firms**

**(a) Testimony**

The Board, and the staff of the Board designated in an order of formal investigation, may issue an accounting board request for the testimony of any person, including any client of a registered public accounting firm, that the Board considers relevant or material to an investigation.

**(1) Requests for Testimony**

An accounting board request for testimony pursuant to subparagraph (a) of this Rule shall –

(i) give appropriate notice, subject to the needs of the investigation of the time and place for the taking of testimony;

(ii) state the method or methods by which the testimony shall be recorded, which may be by sound or sound-and-visual, but shall include by stenographic means; and

(iii) if the person to be examined is an issuer, an association, a governmental agency, or other organized entity, provide a description with reasonable particularity of the matters on which examination is requested.

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**(2) Conduct of Examination and Transcript**

An examination requested pursuant to this Rule shall be conducted consistent with Rules 5102(c) and a transcript shall be prepared consistent with Rule 5102(d). If the person to be examined is an issuer, or a partnership or association or governmental agency, the person to be examined shall designate one or more individuals who consent to testify on its behalf and may set forth, for each individual designated, the matters on which the individual will testify. The individuals so designated shall testify as to matters known or reasonably available to the organization.

**(b) Documents**

The Board, and the staff of the Board designated in an order of formal investigation, may issue an accounting board request to any person, including any issuer, for the production of any document that is relevant or material to an investigation, with appropriate notice, subject to the needs of the investigation. A request issued pursuant to this Rule shall set forth a reasonable time and place for production, subject to the needs of the investigation.

Note: Failure to comply with an accounting board request pursuant to Rule 5105 may result in a Board request for the issuance of a Commission subpoena, pursuant to Rule 5111.

**Rule 5106. Assertion of Claim of Privilege**

**(a) Required Information Supporting Assertion**

When a claim of privilege is asserted in objecting to any accounting board demand for information, including but not limited to testimony or an examination under Rule 5104, and an answer or document is not provided on the basis of such assertion,

(1) the person asserting the privilege, or his or her attorney, shall identify the nature of the privilege (including attorney work product) that is being claimed and indicate the relevant jurisdiction's privilege rule being invoked; and

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(2) the following information shall be provided in the objection, unless divulgence of such information would cause disclosure of the allegedly privileged information –

(i) for documents: (A) the type of document, (e.g., letter or memorandum); (B) the general subject matter of the document; (C) the date of the document; and (D) such other information as is sufficient to identify the document for a Commission subpoena duces tecum, including, where appropriate, the author of the document, the addressees of the document, and any other recipients shown in the document, and, where not apparent, the relationship of the author, addressees, and recipients to each other; and

(ii) for oral communications: (A) the name of the person making the communication and the names of persons present while the communication was made and, where not apparent, the relationship of the persons present to the person making the communication; (B) the date and place of communication; and (C) the general subject matter of the communication.

**(b) Claims During Testimony**

Where a claim of privilege is asserted during testimony, and information is not provided on the basis of such assertion, the information set forth in paragraph (a) shall be furnished –

(1) at the deposition, to the extent it is readily available from the witness or otherwise; or

(2) to the extent the information is not readily available at the deposition, in writing within five business days after the deposition session at which the privilege is asserted, unless otherwise agreed by the staff of the Board.

**(c) Claims Other than During Testimony**

Where a claim of privilege is asserted in response to an accounting board demand for information other than during testimony, the information set forth in paragraph (a) shall be furnished in writing at the time of the response to such accounting board demand, unless otherwise agreed by the Board or its staff.

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**Rule 5107. Uniform Definitions in Demands and Requests for Information**

**(a) General**

The full text of the definitions and rules of construction set forth in paragraphs (c) and (d) is deemed incorporated by reference into all accounting board demands. This Rule shall not preclude (1) the definition of other terms specific to the particular inquiry or investigation, (2) the use of abbreviations, or (3) a more narrow definition of a term defined in paragraph (c).

**(b) Scope**

This Rule is not intended to broaden or narrow the scope of the Board's authority to request information permitted by the Act.

**(c) Definitions**

The following definitions apply to all accounting board demands –

**(1) Communication**

The term "communication" means the transmittal of information (in the form of facts, ideas, inquiries or otherwise).

**(2) Document**

The term "document" is defined to be synonymous in meaning and equal in scope to the usage of this term in Federal Rule of Civil Procedure 34(a), including, without limitation, electronic or computerized data compilations. A draft or non-identical copy is a separate document within the meaning of this term. In no event shall the term "document" be construed to be limited to audit work papers.

**(3) Identify (with respect to person)**

When referring to a person, to "identify" means to give, to the extent known, the person's full name, present or last known address, and when referring to a natural person, additionally, the present or last known place of employment. Once a person

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has been identified in accordance with this subparagraph, only the name of that person need be listed in response to subsequent requests for the identification of that person.

**(4) Identify (with respect to documents)**

When referring to documents, to "identify" means to give, to the extent known, the (i) type of document, (ii) general subject matter, (iii) date of the document; and (iv) author(s), addressee(s) and recipients(s).

**(5) Person**

The term "person" is defined as any natural person or any business, legal or governmental entity or association.

**(6) Concerning**

The term "concerning" means relating to, referring to, describing, evidencing or constituting.

**(d) Rules of Construction**

The following rules of construction apply to all discovery requests –

**(1) All/Each**

The terms "all" and "each" shall be construed as all and each.

**(2) And/Or**

The connectives "and" and "or" shall be construed either conjunctively or disjunctively as necessary to bring within the scope of the request for information all responses that might otherwise be construed outside of its scope.

**(3) Number**

The use of the singular form of any word includes the plural and vice versa.

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**Rule 5108. Confidentiality of Investigatory Records**

(a) Informal inquiries and formal investigations, and any documents, testimony or other information prepared or received by or specifically for the Board or the staff of the Board in connection with such inquiries and investigations, shall be confidential in the hands of the Board, unless and until presented in connection with a public proceeding or released in accordance with Section 105(c) of the Act, and the Board's Rules thereunder; provided, however, that the Board may make such information available –

(1) to the Commission; and

(2) in the discretion of the Board, when determined by the Board to be necessary to accomplish the purposes of the Act or to protect investors, to the following –

(a) the Attorney General of the United States;

(b) the appropriate Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act), other than the Commission, with respect to an audit report for an institution subject to the jurisdiction of such regulator;

(c) State attorneys general in connection with any criminal investigation; and

(d) any appropriate State regulatory authority.

(b) Nothing in paragraph (a) of this rule shall prohibit the Board or the staff of the Board from disclosing any documents, testimony, or other information to any other person as is reasonably necessary to carry out the Board's responsibility, under Section 105 of the Act, to conduct investigations according to fair procedures.

Note: Under Section 105(b)(5) of the Act, the documents described in Rule 5108 "shall be confidential and privileged as an evidentiary matter (and shall not be subject to civil discovery or other legal process) in any proceeding in any federal or State court or administrative agency, and shall be exempt from disclosure, in the hands of an agency or establishment of the federal government, under the Freedom of Information Act (5 U.S.C. 552a), or otherwise, unless and until

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presented in connection with a public proceeding or released in accordance with subsection (c)" of Section 105 of the Act.

Note: The Director of Enforcement and Investigations may engage in and may authorize members of the Board's staff to engage in discussions with persons identified in Rule 5108, or their staff, concerning information obtained in an informal inquiry or a formal investigation.

### **Rule 5109. Rights of Witnesses in Inquiries and Investigations**

#### **(a) Review of Order of Formal Investigation**

Any person who is compelled to testify or produce documents pursuant to a subpoena issued pursuant to Rule 5111, or who testifies or produces documents pursuant to an accounting board demand or request, shall, upon request, be shown the Board's order of formal investigation. In the discretion of the Director of Enforcement and Investigations, a copy of the order of formal investigation may also be furnished to such a person for his or her retention, subject to such limits on dissemination as the Director may require.

#### **(b) Right to Counsel**

Any person compelled to testify pursuant to a subpoena issued pursuant to Rule 5111, or who appears pursuant to an accounting board demand or request, may be accompanied, represented and advised by counsel, subject to Rule 5102(c)(3), provided, however, that the counsel provide the Board's staff with a notice of appearance that states, or state on the record at the commencement of testimony, that the counsel represents the witness.

#### **(c) Inspection and Copying**

Upon written request to the Director of Enforcement and Investigations and proper identification, a witness may inspect the official transcript of the witness's own testimony. Upon written request and payment of the appropriate fees to cover the cost of production or reproduction, a person who has submitted documentary evidence or testimony in an informal inquiry or formal investigation may procure a copy of such evidence or the transcript of such testimony, except that prior to such evidence or testimony being presented in connection with a proceeding or released in accordance

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with Section 105(c) of the Act, and the Board's Rules thereunder, the Director of Enforcement and Investigations may for good cause deny such request.

**(d) Statements of Position**

Registered public accounting firms, and persons associated with firms, who become involved in an informal inquiry or a formal investigation may, on their own initiatives, submit a written statement to the Board setting forth their interests and positions in regard to the subject matter of the investigation. Upon request, the Board's staff, in its discretion, may advise such persons of the general nature of the investigation, including the indicated violations as they pertain to those persons and the amount of time that may be available for preparing and submitting a statement prior to the presentation of a staff recommendation to the Board for the commencement of a disciplinary proceeding. In the event a recommendation for the commencement of a disciplinary proceeding is presented by the staff, any submissions by interested persons will be forwarded to the Board in conjunction with the staff recommendation.

**Rule 5110. Noncooperation with an Investigation**

**(a) Grounds for Instituting Proceedings**

The Board may institute a disciplinary proceeding pursuant to Rule 5200(a)(3) for noncooperation with an investigation if it appears to the Board, on the recommendation of the Director of Enforcement and Investigations or otherwise, that a registered public accounting firm, or a person associated with a such a firm –

- (1) may have failed to comply with an accounting board demand;
- (2) may have knowingly made any false material declaration or made or used any other information, including any book, paper, document, record, recording, or other material, knowing the same to contain any false material declaration;
- (3) may have abused the Board's processes for the purpose of obstructing an investigation; or

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(4) may otherwise have failed to cooperate in connection with an investigation.

**(b) Special and Expedited Procedures**

Disciplinary proceedings instituted pursuant to Rule 5200(a)(3) for noncooperation with an investigation shall be subject to special and expedited procedures as described in Rules 5201(b)(3), 5300(b), 5302(d), 5421(b), 5422(a)(2), 5422(d), 5445(b), and 5460(a)(2)(ii).

**Rule 5111. Requests for Issuance of Commission Subpoenas in Aid of an Investigation**

**(a) General**

The Board may seek issuance by the Commission, in a manner established by the Commission, of a subpoena to require the testimony of, and the production of, any document in the possession of, any person, including any client of a registered public accounting firm, that the Board considers relevant or material to an investigation.

**(b) Application for a Subpoena**

An application for a subpoena submitted to the Commission shall include –

- (1) a completed form of subpoena; and
- (2) such other information as the Commission may require.

**Rule 5112. Coordination and Referral of Investigations**

**(a) Commission Notification of Order of Formal Investigation**

As soon as practicable after entry of an order of formal investigation pursuant to Rule 5101 that involves a potential violation of the securities laws, the Secretary of the Board shall send a copy of the order to the Commission, or any staff of the Commission designated to receive orders of formal investigation by the Board, and Board staff shall thereafter coordinate their work with the work of the Commission's Division of Enforcement, as necessary to protect any ongoing Commission investigation.

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**(b) Board Referrals of Investigations**

The Board may refer any investigation to the Commission and, in the case of an investigation that concerns an audit report for an institution that is subject to the jurisdiction of any other Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act), to such regulator.

**(c) Commission-directed Referrals of Investigations**

At the direction of the Commission, the Board may refer any investigation to –

- (1) the Attorney General of the United States;
- (2) the attorney general of one or more States; and
- (3) an appropriate State regulatory authority.

**Part 2 – Disciplinary Proceedings**

**Rule 5200. Commencement of Disciplinary Proceedings**

**(a) Grounds for Commencement of Disciplinary Proceedings**

The Board may commence a disciplinary proceeding when –

- (1) it appears to the Board, as the result of an investigation or otherwise, that a hearing is warranted to determine whether a registered public accounting firm, or an associated person of such a firm, has engaged in any act or practice, or omitted to act, in violation 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 issued under the Act, or professional standards;

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(2) it appears to the Board, as the result of an investigation or otherwise, that a hearing is warranted to determine whether a registered public accounting firm, or the supervisory personnel of such a firm, has failed reasonably to supervise an associated person, either as required by the Rules of the Board relating to auditing or quality control standards, or otherwise, with a view to preventing violations of this 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, and such associated person commits a violation of the Act, or any of such rules, laws, or standards;

(3) it appears to the Board that a hearing is warranted pursuant to Rule 5110.

**(b) Appointment of a Hearing Officer**

As soon as practicable after the Board has issued an order instituting proceedings, or after a registration applicant has requested a hearing pursuant to Rule 5500(b), the Secretary shall assign a hearing officer to preside over the proceeding and shall serve the parties with notice of the hearing officer's assignment. Subject to Rules 5402 and 5403, the hearing officer shall have the authority to do all things necessary and appropriate to discharge his or her duties. The powers of the hearing officer include, but are not limited to, the following –

- (1) obtaining a court reporter to administer oaths and affirmations;
- (2) issuing accounting board demands pursuant to Rule 5424;
- (3) receiving relevant evidence and ruling upon the admission of evidence and offers of proof;
- (4) regulating the course of a proceeding and the conduct of the parties and their counsel;
- (5) holding prehearing and other conferences and requiring the attendance at any such conference of at least one representative of each party who has authority to negotiate concerning the resolution of issues in controversy;

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(6) recusing himself or herself upon motion made by a party or upon his or her own motion;

(7) ordering, in his or her discretion, in a proceeding involving more than one respondent, that the interested division indicate, on the record, at least one day prior to the presentation of any evidence, each respondent against whom that evidence will be offered;

(8) subject to any limitations set forth elsewhere in these Rules, considering and ruling upon all procedural and other motions;

(9) preparing an initial decision as provided in Rule 5204;

(10) upon notice to all parties, reopening any hearing prior to the filing of an initial decision therein, or, if no initial decision is to be filed, prior to the time fixed for the filing of final briefs with the Board;

(11) informing the parties as to the availability of one or more alternative means of dispute resolution, and encouraging the use of such methods; and

(12) scheduling hearing dates, except that a hearing officer may not, absent the approval of the Board, change a hearing date set by Board order.

**(c) Separation of Functions**

The staff of the Division of Enforcement and Investigations may not participate or advise in the decision, or in Board review of the decision, in any proceeding in which the Division of Enforcement and Investigations is the interested division, except as a witness or counsel in the proceeding. Any other employee or agent of the Board engaged in the performance of investigative or prosecutorial functions for the Board in a proceeding may not, in that proceeding or one that is factually related, participate or advise in the decision, or in Board review of the decision, except as a witness or counsel in the proceeding. A hearing officer may not be responsible to or subject to the supervision or direction of an employee or agent engaged in the performance of investigative or prosecuting functions for the Board.

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**(d) Consolidation of Proceedings**

By order of the Board or a hearing officer, proceedings involving a common question of law or fact may be consolidated for hearing of any or all the matters at issue in such proceedings. The Board or the hearing officer may make such orders concerning the conduct of such proceedings as it deems appropriate to avoid unnecessary cost or delay. Consolidation shall not prejudice any rights under these Rules and shall not affect the right of any party to raise issues that could have been raised if consolidation had not occurred. For purposes of this Rule, no distinction is made between joinder and consolidation of proceedings.

**Rule 5201. Notification of Commencement of Disciplinary Proceedings**

**(a) Notice**

Whenever an order instituting proceedings is issued by the Board, the Secretary shall give each firm or person charged appropriate notice of the order within a time reasonable in light of the circumstances. If the order instituting proceedings sets a hearing date, each party shall be given notice of the hearing within a time reasonable, in light of the circumstances, in advance of the hearing.

Note: Paragraph (a) requires that appropriate notice of an order instituting proceedings be given. Where emergency or expedited action is sought, notice of a hearing may be given prior to formal service of the order instituting proceedings by any means calculated to give actual notice that a hearing will be held.

**(b) Content of Order Instituting Proceedings**

An order instituting proceedings issued pursuant to subparagraph (a) shall include a short and plain statement of the matters of fact and law to be considered and determined with respect to each person charged, including –

(1) in the case of a proceeding instituted pursuant to Rule 5200(a)(1) –

(i) the conduct alleged to have violated the Act, the Rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports or the obligations and liabilities of accountants with respect thereto, including the rules of the Commission under the Act and professional standards; and

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(ii) the rule, statute or standard violated;

(2) in the case of a proceeding instituted pursuant to Rule 5200(a)(2) –

(i) the failure to supervise alleged to have violated the Rules of the Board or to have failed to prevent violations of the Act, the Rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports or the obligations and liabilities of accountants with respect thereto, including the rules of the Commission under the Act and applicable professional standards; and

(ii) the violative conduct of the supervised associated person and the rule, statute or standard violated; or

(3) in the case of a proceeding instituted pursuant to Rule 5200(a)(3) –

(i) the conduct alleged to constitute the failure to cooperate with an investigation; and

(ii) a hearing date.

**(c) Notice of a Hearing on a Registration Application**

In the case of a proceeding pursuant to Rule 5500, the notice of a hearing shall state proposed grounds for disapproving the registration application.

**(d) Amendment to Order Instituting Proceedings**

**(1) By the Board**

Upon motion by the interested division, the Board may, at any time, amend an order instituting proceedings, or a notice of a hearing, to include new matters of fact or law.

**(2) By the Hearing Officer**

Upon motion by the interested division, the hearing officer may, at any time prior to the filing of an initial decision or, if no proposed initial decision is to be filed, prior to

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the time fixed for the filing of final briefs with the Board, amend an order instituting proceedings to include new matters of fact or law that are within the scope of the original order instituting proceedings.

Note: Where amendments to an order instituting proceedings are intended to correct an error, to conform the order to the evidence or to take into account subsequent developments which should be considered in disposing of the proceeding, and the amendments are within the scope of the original order, either a hearing officer or the Board has authority to amend the order. Since, however, the Board has not delegated its authority to authorize orders instituting proceedings, hearing officers do not have authority to initiate new charges or to expand the scope of matters set down for hearing beyond the framework of the original order instituting proceedings.

## **Rule 5202. Record of Disciplinary Proceedings**

### **(a) Contents of the Record**

#### **(1) Record of a Disciplinary Proceeding**

A hearing record shall consist of –

(i) the order instituting proceedings, each notice of hearing and any amendments;

(ii) each application, supplemental application, motion, submission or other paper, and any amendments, motions, objections, and exceptions to or regarding them;

(iii) each stipulation, transcript of testimony and document or other information admitted into evidence;

(iv) each written communication accepted by the hearing officer pursuant to Rule 5420;

(v) with respect to a request to disqualify a hearing officer or to allow the hearing officer's withdrawal pursuant to Rule 5402, each affidavit or transcript of testimony taken and the decision made in connection with the request;

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- (vi) all motions, briefs and other papers filed on interlocutory appeal;
- (vi) any proposed findings and conclusions;
- (viii) each written order or notice issued by the hearing officer or the Board; and
- (ix) any other document or item accepted into the record by the Board or the hearing officer.

**(2) Record on Disapproval of Application for Registration**

The record on a disapproval of an application with respect to which the applicant has elected to waive its opportunity for a hearing pursuant to Rule 5500 shall consist of –

- (i) the application for registration, and any supplemented application;
- (ii) any additional information provided by the applicant;
- (iii) any other information obtained by the Board in connection with the application;
- (iv) the notice of a hearing and any written order issued by the Board; and
- (v) any other document or item accepted into the record by the Board.

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**(b) Documents Not Admitted**

Any document offered in evidence but excluded, and any document marked for identification but not offered as an exhibit, shall not be considered a part of the record. The Secretary shall retain any documents offered in evidence but excluded until all opportunities for Commission and judicial review have been exhausted or waived.

**(c) Substitution of Copies**

A true copy of a document may be substituted for any document in the record or any document retained pursuant to paragraph (b) of this Rule.

**(d) Preparation of Record and Certification of Record Index**

Promptly after the close of a hearing, the hearing officer shall transmit to the Secretary an index of any motions, exhibits or any other documents submitted to, or accepted into evidence by, the hearing officer that have not been previously transmitted to the Secretary, and the Secretary shall prepare a record index. Prior to issuance of an initial decision, the Secretary shall transmit the record index to the hearing officer and serve a copy of the record index on each party. Any party may file proposed corrections to the record index with the hearing officer within 15 days of service of the record index. The hearing officer shall, by order, direct whether any corrections to the record index shall be made. The Secretary shall make such corrections, if any, and issue a revised record index. The initial decision shall include a certification that the record consists of the items set forth in the record index or revised record index issued by the Secretary.

**(e) Final Transmittal of Record Items to the Secretary**

After the close of a hearing, the hearing officer shall transmit to the Secretary originals of exhibits or any other documents submitted to, or accepted into evidence by, the hearing officer, and any other portions of the record that have not already been transmitted to the Secretary. Prior to service of the initial decision by the Secretary, the Secretary shall inform the hearing officer if any portions of the record are not in the Secretary's custody.

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**Rule 5203. Public and Private Hearings**

No hearing shall be public unless ordered by the Board. In any proceeding commenced pursuant to Rule 5200(a), the Board shall not order that a hearing be public except for good cause shown and with consent of the parties.

**Rule 5204. Determinations in Disciplinary Proceedings**

**(a) Burden of Proof**

In any disciplinary proceeding instituted pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5200(a)(3), the interested division shall bear the burden of proving an alleged violation or failure to supervise by a preponderance of the evidence.

**(b) Initial Decision of a Hearing Officer**

Unless the Board directs otherwise, a hearing officer shall prepare an initial decision in any proceeding in which the Board directs a hearing officer to preside at a hearing. An initial decision shall include findings and conclusions, including sanctions, if appropriate, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record and such other information as the Board may require.

Note: Unless the Board has directed otherwise, the Board expects hearing officers in proceedings instituted pursuant to Rule 5200(a)(1) or Rule 5200(a)(2) to prepare initial decisions within 60 days after the deadline for filing post-hearing briefs or other submissions; the Board expects hearing officers in proceedings instituted pursuant to Rule 5200(a)(3) to prepare initial decisions within 30 days after deadline for filing post-hearing briefs; and the Board expects hearing officers in proceedings pursuant to Rule 5500 to prepare initial decisions within 45 days after the deadline for filing post-hearing briefs or other submissions.

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**(c) Filing, Service and Publication**

The hearing officer shall file the initial decision with the Secretary. The Secretary shall promptly serve the initial decision upon the parties. In a public proceeding, the Secretary shall as soon as practicable thereafter publish the initial decision, unless the Board otherwise directs.

**(d) When Final**

(1) An initial decision as to a party shall become the final decision of the Board as to that party upon issuance of a notice of finality by the Secretary.

(2) Subject to subparagraph (3) of this paragraph, the Secretary shall issue a notice of finality no later than 20 days after the lapsing of the time period for filing a petition for review of the initial decision.

(3) The Secretary shall not issue a notice of finality as to any party

(i) who has filed a timely petition for review; or

(ii) with respect to whom the Board has ordered review of the initial decision pursuant to Rule 5460(b).

**Rule 5205. Settlement of Disciplinary Proceedings Without a Determination After Hearing**

**(a) Availability**

Any firm or person who is notified that a proceeding may or will be instituted against him or her, or any firm or person that is a party to a proceeding already instituted, may, at any time, propose in writing an offer of settlement.

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**(b) Procedure**

An offer of settlement shall state that it is made pursuant to this Rule; shall recite or incorporate as a part of the offer the provisions of paragraphs (c)(2) and (3) of this Rule; shall be signed by the person making the offer, not by counsel; and shall be submitted to the Director of Enforcement and Investigations.

**(c) Consideration of Offers of Settlement**

(1) The Director of Enforcement and Investigations shall present an offer of settlement to the Board with his or her recommendation, except that, if the recommendation is unfavorable, the offer shall not be presented to the Board unless the person making the offer so requests.

(2) By submitting an offer of settlement, the person making the offer waives, subject to acceptance of the offer –

(i) all hearings pursuant to the statutory provisions under which the proceeding is to be or has been instituted;

(ii) the filing of post-hearing briefs or other submissions, proposed findings of fact and conclusions of law;

(iii) proceedings before, and an initial decision by, a hearing officer;

(iv) all post-hearing procedures; and

(v) judicial review by any court.

(3) By submitting an offer of settlement the person further waives –

(i) such provisions of the Rules of Board Procedure or other requirements of law as may be construed to prevent any member of the Board's staff from participating in the preparation of, or advising the Board as to, any order, opinion, finding of fact, or conclusion of law to be entered pursuant to the offer; and

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(ii) any right to claim bias or pre-judgment by the Board based on the consideration of or discussions concerning settlement of all or any part of the proceeding.

(4) If the Board rejects the offer of settlement, the person making the offer shall be notified of the Board's action and the offer of settlement shall be deemed withdrawn. The rejected offer shall not constitute a part of the record in any proceeding against the person making the offer. Rejection of an offer of settlement does not affect the continued validity of waivers pursuant to paragraph (c)(3) of this Rule with respect to any discussions concerning the rejected offer of settlement.

(5) Final acceptance of any offer of settlement will occur only upon the issuance of findings and an order by the Board.

Note: In a hearing on disapproval of registration, an offer of settlement will be considered and handled by the Director of Registration and Inspections in accordance with Rule 5206 as if the Director of Registration and Inspections were the Director of Enforcement and Investigations.

#### **Rule 5206. Automatic Stay of Final Disciplinary Actions**

No final disciplinary sanction of the Board shall be effective until the later of –

(a) Commission action to dissolve the stay provided by Section 105(e) of the Act; or

(b) the expiration of the period during which, on its own motion, or upon application pursuant to Section 19(d)(2) of the Exchange Act, the Commission may institute review of the sanction.

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### **Part 3 – Disciplinary Sanctions**

#### **Rule 5300. Sanctions**

##### **(a) Sanctions in Proceedings Instituted Pursuant to Rule 5200(a)(1) or Rule 5200(a)(2)**

If the Board finds, based on all of the facts and circumstances, that a registered public accounting firm or associated person thereof has engaged in any act or practice, or omitted to act, in violation 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 issued under the Act, or professional standards, the Board may impose such disciplinary or remedial sanctions as it determines appropriate, subject to the applicable limitations under Section 105(c)(5) of the Act, including –

- (1) temporary suspension or permanent revocation of registration;
- (2) temporary or permanent suspension or bar of a person from further association with any registered public accounting firm;
- (3) temporary or permanent limitation on the activities, functions or operations of such firm or person (other than in connection with required additional professional education or training);

Note: Limitations on the activities, functions or operations of a firm may include prohibiting a firm from accepting new audit clients for a period of time, requiring a firm to assign a reviewer or supervisor to an associated person, requiring a firm to terminate one or more audit engagements, and requiring a firm to make functional changes in supervisory personnel organization and/or in engagement team organization.

- (4) a civil money penalty for each such violation, in an amount equal to –
  - (i) not more than \$100,000 for a natural person or \$2,000,000 for any other person; and

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(ii) in any case to which Section 105(c)(5) of the Act applies, not more than \$750,000 for a natural person or \$15,000,000 for any other person;

(5) censure;

(6) require additional professional education or training;

(7) require a registered public accounting firm to engage an independent monitor, subject to the approval of the Board, to observe and report on the firm's compliance with 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, or professional standards;

(8) require a registered public accounting firm to engage counsel or another consultant to design policies to effectuate compliance with 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, or professional standards;

(9) require a registered public accounting firm, or a person associated with such a firm, to adopt or implement policies, or to undertake other actions, to improve audit quality or to effectuate compliance with 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, or professional standards; and

(10) require a registered public accounting firm to obtain an independent review and report on one or more engagements.

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**(b) Sanctions in Proceedings Instituted Pursuant to Rule 5200(a)(3)**

If the Board finds, based on all of the facts and circumstances, that a registered public accounting firm, or a person associated with such a firm, has failed to comply with an accounting board demand, has given false testimony or has otherwise failed to cooperate in an investigation, the Board may impose such disciplinary or remedial sanctions as it determines appropriate, including –

(1) the sanctions described in subparagraphs (1) – (5) of paragraph (a) of this Rule;

(2) requiring a registered public accounting firm to engage a special master or independent monitor, appointed by the hearing officer, to monitor and report on the firms' compliance with an accounting board demand or with future accounting board demands; or

(3) authorizing the hearing officer to retain jurisdiction to monitor compliance with an accounting board demand or with future account board demands and to rule on future disputes, if any, related to such demands.

Note: Rule 5300 does not preclude the imposition of any sanction, on consent, in the context of a settlement, notwithstanding that the sanction is not listed in the Rule.

**Rule 5301. Effect of Sanctions**

**(a) Effect on Persons**

No person that is suspended or barred from being associated with a registered public accounting firm, or has failed to comply with any sanction pursuant to Rule 5300, may willfully become or remain associated with any registered public accounting firm, without the consent of the Board, pursuant to Rule 5302, or the Commission.

Note: A person who is suspended or barred from being associated with a registered public accounting firm may not, in connection with the preparation or issuance of any audit report, (i) share in the profits of, or receive compensation in any other form from, any registered public accounting firm, or (ii) participate as agent on behalf of such a firm in any activity of that firm. See Rule 1001(p)(i).



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**(b) Effect on Registered Public Accounting Firms**

No registered public accounting firm that knows, or, in the exercise of reasonable care should have known, of the suspension or bar of a person may permit such person to become or remain associated with it, without the consent of the Board, pursuant to Rule 5302, or the Commission.

Note: Rule 5301(b) prohibits a registered public accounting firm from permitting a person subject to a suspension or bar, in connection with the preparation or issuance of any audit report, to (i) share in the profits of, or receive compensation in any other form from, such firm, or (ii) participate as agent on behalf of such a firm in any activity of that firm. See Rule 1001(p)(i).

**Rule 5302. Applications for Relief From, or Modification of, Revocations and Bars**

**(a) Application for Registration After a Revocation of Registration**

Unless the Board orders otherwise, any public accounting firm whose registration has been revoked pursuant to a Board determination that permitted the firm an opportunity to reapply for registration after a specified time period has lapsed may file an application for registration pursuant to Rule 2101 after the specified time period has lapsed. The revocation of the firm's registration shall continue, however, unless and until an application for registration is approved pursuant to Rule 2106(b)(1).

**(b) Petition to Terminate a Bar**

**(1) Scope**

Any person subject to a bar imposed by an order that contains a proviso that a petition to terminate the bar may be made to the Board after a specific period of time may file a petition for Board consent to associate, or to change the terms and conditions of association, with a registered public accounting firm.

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**(2) Form of Petition**

A petition to terminate a bar shall be supported by an affidavit that addresses the factors set forth in subparagraph (b)(4) of this Rule and shall include as exhibits –

- (i) a copy of the Board order imposing the bar;
- (ii) a copy of any Commission or court order concerning the bar;
- (iii) a written statement by the proposed registered public accounting firm with which the petitioner wishes to associate that describes –
  - (A) the terms and conditions of employment and supervision to be exercised over such petitioner and, where applicable, by such petitioner;
  - (B) the qualifications, experience, and disciplinary records of the proposed supervisor(s) of the petitioner;
  - (C) the compliance and disciplinary history, during the two years preceding the filing of the petition, of the registered public accounting firm with which the petitioner wishes to be associated; and
  - (D) the names of any other associated persons in the same registered public accounting firm who have previously been barred by the Board or the Commission, and whether they are to be supervised by the petitioner.

**(3) Required Showing**

The petitioner shall make a showing satisfactory for the Board to be able to determine that the proposed association would be consistent with the public interest.

**(4) Factors to be Addressed**

The affidavit required by paragraph (b)(2) of this Rule shall address each of the following –

- (i) the time period since the imposition of the bar;

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- (ii) any restitution or similar action taken by the petitioner to recompense any person injured by the misconduct that resulted in the bar;
- (iii) the petitioner's compliance with the order imposing the bar;
- (iv) the petitioner's employment during the period subsequent to the imposition of the bar;
- (v) the capacity or position in which the applicant proposes to be associated;
- (vi) the manner and extent of supervision to be exercised over such petitioner and, where applicable, by such petitioner;
- (vii) any relevant courses, seminars, examinations or other actions completed by the applicant subsequent to imposition of the bar to prepare for his or her reassociation; and
- (viii) any other information material to the petition.

**(5) Notification to Petitioner and Written Statement**

In the event an adverse recommendation is proposed by the staff with respect to an application made pursuant to this rule, the applicant shall be so advised and provided with a written statement of the reasons for such recommendation. The applicant shall have 30 days to submit a written statement in response.

**(c) Application for Termination of Other Revocations and Bars**

Unless the Board orders otherwise, any firm or person that is subject to a revocation or bar pursuant to a Board determination that does not provide for an opportunity to reapply for registration, or to terminate a bar, may request leave to file an application for registration, or a petition to terminate a bar, at any time. The sanction shall continue, however, unless and until the Board has permitted and granted such an application or petition for good cause shown.

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**(d) Application for Termination of Sanctions for Noncooperation**

Unless the Board orders otherwise, any firm or person that has remedied the noncooperation that formed the basis for a disciplinary sanction may file an application for termination of any such sanction that is ongoing. The sanction shall continue, however, unless and until it has been terminated by the Board.

**(e) Applications for Termination of Other Sanctions**

Unless the Board orders otherwise, any firm or person subject to a sanction pursuant to subparagraphs (3), (6), (7), (8), (9) or (10) of Rule 5300(a) may file an application for termination of any continuing sanction at any time, and the applicant may, in the Board's discretion, be afforded a hearing. The sanction shall continue, however, unless and until it has been terminated by the Board for good cause shown.

**Rule 5303. Use of Money Penalties**

Subject to the availability in advance in an appropriations act, all civil money penalties shall be used to fund a merit scholarship program for undergraduate and graduate students enrolled in accredited accounting degree programs, administered by the Board or by an entity or agent identified by the Board.

**Rule 5304. Summary Suspension for Failure to Pay Money Penalties**

**(a) Registered Public Accounting Firms**

If, thirty days after exhaustion of all reviews and appeals, and the termination of any stay authorized by law or the Rules of the Board, a registered public accounting firm has failed to pay a money penalty imposed pursuant to Rule 5300(a)(4), the Board may, after seven days' notice in writing, summarily suspend the registration of the registered public accounting firm. Such a suspension of registration shall lapse upon payment, within 90 days, of the money penalty, plus interest. If payment is not made within 90 days, a suspension of registration shall be lifted only upon –

- (1) payment of the money penalty, plus interest; and

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(2) the filing of an application for registration pursuant to Rule 2101, and Board approval of that application pursuant to the Board's Rules relating to registration.

**(b) Associated Persons**

If, thirty days after exhaustion of all reviews and appeals, and the termination of any stay, authorized by law or the Rules of the Board, an associated person has failed to pay a money penalty imposed pursuant to Rule 5300(a)(4), the Board may, after seven days' notice in writing, summarily suspend the associated person. If such a money penalty is not paid within 90 days of such notice, the Board may summarily bar such person.

**Part 4 – Rules of Board Procedure**

**GENERAL**

**Rule 5400. Hearings**

Hearings for the purpose of taking evidence shall be held only upon order of the Board. All hearings shall be conducted in a fair, impartial, expeditious and orderly manner.

**Rule 5401. Appearance and Practice Before the Board**

A person shall not be represented before the Board or a hearing officer except as stated in paragraphs (a) or (b) of this Rule or as otherwise permitted by the Board or a hearing officer.

**(a) Representing Oneself**

In any proceeding, an individual may appear on his or her own behalf.

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**(b) Representing Others**

In any proceeding, a person may be represented by counsel; a member of a partnership may represent the partnership; a bona fide officer of a corporation, trust or association may represent the corporation, trust or association.

**(c) Designation of Address for Service; Notice of Appearance; Power of Attorney; Withdrawal**

**(1) Representing Oneself**

When an individual first makes any filing or otherwise appears on his or her own behalf before the Board or a hearing officer, he or she shall file with the Secretary both an electronic and a mailing address at which any notice or other written communication required to be served upon him or her or furnished to him or her may be sent and a telephone number where he or she may be reached during business hours, and the individual shall promptly advise the Secretary of changes to that information during the course of the proceeding.

**(2) Representing Others**

When a person first makes any filing or otherwise appears in a representative capacity before the Board or a hearing officer, that person shall file with the Secretary, and keep current, a written notice stating the name of the proceeding; the representative's name, mailing address, electronic address and telephone number; and the name and electronic and mailing addresses of the person or persons represented; and, if the person is an attorney, a declaration that the attorney is admitted to practice before the Supreme Court of the United States or the highest court of any state, as defined in Section 3(a)(16) of the Exchange Act.

**(3) Power of Attorney**

Any individual appearing or practicing before the Board in a representative capacity may be required to file a power of attorney with the Board showing his or her authority to act in such capacity.

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**(4) Withdrawal**

Withdrawal by any individual appearing in a representative capacity shall be permitted only by order of the Board or the hearing officer. A motion seeking leave to withdraw shall state with specificity the reasons for such withdrawal. Leave to withdraw shall not be withheld absent good cause.

**Rule 5402. Hearing Officer Disqualification and Withdrawal**

**(a) Motion for Withdrawal**

A party who has a reasonable, good faith basis to believe that a hearing officer has a conflict of interest or personal bias, or circumstances otherwise exist such that the hearing officer's fairness may reasonably be questioned, may make a motion to the hearing officer that the hearing officer withdraw, which shall be filed with the Secretary. The motion shall be accompanied by an affidavit setting forth in detail the facts alleged to constitute grounds for disqualification. If the hearing officer finds himself or herself not disqualified, he or she shall so rule and shall continue to preside over the proceeding. A motion for withdrawal shall be filed within 15 days after the later of –

- (1) when the party learned of the facts believed to constitute the basis for the disqualification; or
- (2) when the party was notified of the assignment of the hearing officer.

**(b) Appointment of a Replacement Hearing Officer**

Upon withdrawal of a hearing officer, or in the event that a hearing officer is incapacitated or is otherwise unable to continue to serve after being appointed, the Secretary will appoint a replacement hearing officer. To ensure fairness to the parties and expedite completion of the proceeding when a replacement hearing officer is appointed after a hearing has commenced, the replacement hearing officer may recall any witness or may certify familiarity with any part or all of the record.

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**Rule 5403. Ex Parte Communications**

Except to the extent permitted for the disposition of ex parte matters as authorized by law or the Board's Rules –

(a) the person presiding over an evidentiary hearing may not consult a person or party on a fact in issue, unless on notice and with opportunity for all parties to participate; and

(b) neither a party, nor any Board staff that substantially assists the interested division on the particular matter, whether before or during the hearing, may –

(1) communicate with the person presiding over an evidentiary hearing on a fact in issue, unless on notice and opportunity for all parties to participate; or

(2) communicate with the Board or any member of the Board on a fact in issue, unless on notice and opportunity for all parties to participate or under circumstances in which a party excluded from the communication has waived the rights described in Rule 5205(c)(3) with respect to the matters that are the subject of the communication.

**Rule 5404. Service of Papers by Parties**

In every proceeding, each paper, including each notice of appearance, written motion, brief, or other written communication, shall be served upon each party in a manner calculated to bring the paper to the attention of the party to be served.

**Rule 5405. Filing of Papers With the Board: Procedure**

**(a) When to File**

All papers required to be served by a party upon any person shall be filed with the Board at the time of service or promptly thereafter. Papers required to be filed with the Board must be received within the time limit, if any, for such filing.

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**(b) Where to File**

Unless otherwise permitted by the Secretary, filing of papers with the Board shall be made by electronically filing them with the Secretary.

Note: When a document has been filed electronically, the official record is the electronic recording of the document as stored by the Secretary, and the filing party is bound by the document as filed. A document filed electronically is deemed filed at the date received electronically by the Secretary. Upon request, the Secretary may permit regulators granted permission to participate on a limited basis (to request a stay), amici curiae, nonparties and others to file in paper form. Where practicable, the Secretary will scan such a filing into the docket file.

**Rule 5406. Filing of Papers: Form**

**(a) Specifications**

Papers filed in connection with any proceeding shall –

(1) be formatted in a Portable Document Format on pages measuring 8½ x 11 inches, except that, upon consent of the Secretary for good cause, a document may be filed in paper form;

Note: To the extent that the reduction of larger documents would render them illegible, the Secretary may consent to the filing of such documents on larger paper, in electronic or paper form.

(2) include at the head of the paper, or on a title page, the name of the Board, the title of the proceeding, the names of the parties, the subject of the particular paper or pleading, and the file number assigned to the proceeding;

(3) be paginated with margins at least 1 inch wide; and

(4) be double-spaced in a 12-point font, with single-spaced footnotes and single-spaced indented quotations.

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**(b) Form of Briefs**

All briefs containing more than 10 pages shall include a table of contents, an alphabetized table of cases, a table of statutes, and a table of other authorities cited, with references to the pages of the brief wherein they are cited.

**Rule 5407. Filing of Papers: Signature Requirement and Effect**

Following the issuance of an order instituting proceedings, every filing of a party who represents himself or herself shall sign his or her individual name and state the date and his or her address and telephone number on every filing. A party represented by counsel shall be signed by at least one counsel of record in his or her name and shall state that counsel's business address and telephone number.

Note: If practicable, a party's or an attorney's signature should be scanned into an electronic document. In any event, however, the use of an attorney's electronic mail address, or password for the Board's electronic filing system, shall constitute the signature of that attorney.

**Rule 5408. Motions**

**(a) Generally**

Unless made during a hearing or conference, a motion shall be in writing, shall state with particularity the grounds therefor, shall set forth the relief or order sought, and shall be accompanied by a written brief of the points and authorities relied upon. Unless otherwise ordered by the Board or the hearing officer, if a motion is properly made to the Board concerning a proceeding to which a hearing officer is assigned, the proceeding before the hearing officer shall continue pending the determination of the motion by the Board. No oral argument shall be heard on any motion unless the Board or the hearing officer otherwise directs.

**(b) Opposing and Reply Briefs**

Except as provided in Rule 5427, and unless otherwise ordered by the Board or a hearing officer, a brief in opposition to a motion shall be filed within five days after service of the motion. Reply briefs are only permitted with leave of the hearing officer.

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**(c) Length Limitation**

Except as provided in Rule 5427, a brief in support of or opposition to a motion shall not exceed 10 pages, exclusive of pages containing any table of contents, table of authorities, and/or addendum. The hearing officer may grant requests for leave to file briefs in excess of 10 pages, upon a showing of good cause.

**Rule 5409. Default and Motions to Set Aside Default**

**(a) Default**

A party to a proceeding may be deemed to be in default and the Board or the hearing officer may determine the proceeding against that party upon consideration of the record, including the order instituting proceedings or notice of a hearing, the allegations of which may be deemed to be true, if that party fails –

(1) to appear, in person or through a representative, at a hearing or conference of which that party has been notified;

(2) to answer when required to do so by a Board order, to respond to a dispositive motion within the time provided, or otherwise to defend the proceeding; or

(3) to cure a deficient filing within the time specified by the Board or the hearing officer.

**(b) Motion to Set Aside Default**

A motion to set aside a default shall be made within a reasonable time, state the reasons for the failure to appear or defend, and specify the nature of the proposed defense in the proceeding. In order to prevent injustice and on such conditions as may be appropriate, the hearing officer, at any time prior to the filing of the initial decision, or the Board at any time, may for good cause shown set aside a default.

**Rule 5410. Additional Time For Service by Mail**

If service is made by mail, three days shall be added to the prescribed period for response.

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**Rule 5411. Modifications of Time, Postponements and Adjournments**

Except as otherwise provided by law, the Board, at any time, or the hearing officer, at any time prior to the filing of his or her initial decision, may, for good cause shown, extend or shorten any time limits prescribed by these Rules for the filing of any papers and may, consistent with paragraph (b) of this Rule, postpone or adjourn any hearing.

**Rules 5412. – 5419. [Reserved]**

**PREHEARING RULES**

**Rule 5420. Stay Requests**

**(a) Leave to Participate to Request a Stay**

The Board or the hearing officer may grant leave to participate on a limited basis only to an authorized representative of the Commission, an authorized representative of the United States Department of Justice, an authorized representative of a United States Attorney, an appropriate state regulatory authority, or an authorized representative of any criminal prosecutorial authority of any State or any other political subdivision of a State for the purpose of requesting a stay during the pendency of a Commission investigation or proceeding, a criminal investigation or prosecution, or a state regulatory proceeding, arising out of the same or similar facts that are at issue in the pending Board or disciplinary proceeding. Motions for leave to participate shall be in writing, shall set forth the nature and extent of the movant's interest in the proceeding, and, except where good cause for late filing is shown, shall be filed not later than 20 days prior to the date fixed for the commencement of the hearing. A stay granted pursuant to this Rule may be granted for such a period and upon such conditions as the Board or the hearing officer deems appropriate.

**(b) Stay to Protect Ongoing Commission Investigation**

Upon a showing that a stay requested pursuant to this Rule is necessary to protect an ongoing Commission investigation, the motion for the stay shall be granted.

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**(c) Other Stays**

Upon a showing that such a stay is in the public interest or for the protection of investors, the motion for the stay shall be favored.

**Rule 5421. Answer to Allegations**

**(a) When Required**

In its order instituting proceedings, the Board may require any party to file an answer to each of the allegations contained therein. Even if not so ordered, any party in any proceeding may elect to file an answer.

**(b) When to File**

Unless additional time is granted by the hearing officer or the Board, a party filing an answer as provided in paragraph (a) of this Rule shall do so within 20 days after service upon the party of an order instituting proceedings pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5500, and within 5 days after service upon the party of an order instituting proceedings pursuant to Rule 5200(a)(3). If the order instituting proceedings is amended, the Board or the hearing officer may require that an amended answer be filed and, if such an answer is required, shall specify a date for the filing thereof.

**(c) Contents of Answer and Effect of Failure to Deny**

Unless otherwise directed by the hearing officer or the Board, an answer shall specifically admit, deny, or state that the party does not have, and is unable to obtain, sufficient information to admit or deny each allegation in the order instituting proceedings. When a party intends in good faith to deny only a part of an allegation, the party shall specify so much of it as is true and shall deny only the remainder. A statement of a lack of information shall have the effect of a denial. A defense of res judicata, statute of limitations or any other matter constituting an affirmative defense shall be asserted in the answer. Any allegation not denied shall be deemed admitted.

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**Rule 5422. Availability of Documents For Inspection and Copying**

**(a) Documents to be Available for Inspection and Copying**

**(1) Proceedings Commenced Pursuant to Rule 5200(a)(1) and 5200(a)(2)**

Unless otherwise provided by this Rule, or by order of the Board or the hearing officer, in proceedings pursuant to Rule 5200(a)(1) or Rule 5200(a)(2), the Division of Enforcement and Investigations shall make available for inspection and copying by any party to the proceeding –

(i) each request, subpoena, or accounting board demand for documents, testimony, or information issued in the investigation or in the informal inquiry, if any, that preceded the investigation or disciplinary proceeding;

(ii) responses to any such requests, subpoenas, and accounting board demands, including any documents produced in response;

(iii) testimony transcripts and exhibits, and any other verbatim records of witness statements;

(iv) all other documents prepared or obtained by the Division of Enforcement and Investigations in connection with the investigation prior to the institution of proceedings, except that the Division need not produce any documents described in subparagraph (b) that it does not intend to introduce as evidence.

**(2) Proceedings Commenced Pursuant to Rule 5200(a)(3)**

Unless otherwise provided by this Rule, or by order of the Board, the Division of Enforcement and Investigations shall make available for inspection and copying by any party to the proceeding all documents upon which the Division intends to rely in seeking a finding of noncooperation but shall not be required to make available any other documents.

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**(3) Proceedings Commenced Pursuant to Rule 5500**

Unless otherwise provided by this Rule, or by order of the Board or the hearing officer, in proceedings pursuant to Rule 5500, the Division of Registration and Inspections shall make available for inspection and copying by the applicant documents obtained by that division in connection with the registration application prior to the notice of hearing, except that the Division need not produce any documents described in subparagraph (b) that it does not intend to introduce as evidence.

**(b) Documents That May Be Withheld**

(1) The interested division may decline to make available for inspection and copying –

(i) any document prepared by a member of the Board or of the Board's staff that has not been disclosed to any person other than Board members, Board staff, or persons retained by the Board or Board staff to provide services in connection with the investigation, disciplinary proceeding, or hearing on disapproval of registration;

(ii) any other document that is privileged, including any other document protected by the attorney work product doctrine;

(iii) any document that would disclose the identity of a confidential source; and

(iv) any other document that the staff identifies for the hearing officer's consideration as to whether the document may be withheld as not relevant to the subject matter of the proceeding or otherwise for good cause shown.

(2) Nothing in this paragraph (b), or in paragraph (a)(2) above, authorizes the interested division in connection with a disciplinary proceeding or hearing on disapproval of registration to withhold documents that contain material exculpatory evidence.

**(c) Procedures Concerning Withheld Documents**

(1) The interested division shall, at the time it makes documents available to a respondent under this rule, provide the respondent with a log of

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documents withheld pursuant to paragraph (b)(1)(ii) of this Rule. The log shall provide the same information that a person would be required to supply to the Board under Rule 5106 in connection with a privilege assertion. On a motion by any respondent, a hearing officer may, in his or her discretion, require the interested division to submit any document listed on the log for inspection by the hearing officer in camera. A hearing officer may order that any such document be made available to a respondent for inspection and copying only if the hearing officer determines that the document is not a document described in paragraph (b)(1)(ii).

(2) The interested division shall, at the time it makes documents available to a respondent under this rule, provide the hearing officer and each respondent with a list of documents withheld pursuant to paragraph (b)(1)(iii) or (b)(1)(iv) of this Rule and a brief description of the reason for withholding each document. The list provided to the respondent may be redacted as necessary to protect interests related to the interested division's reason for withholding the document. The hearing officer may require the interested division to submit any such document for inspection by the hearing officer in camera. The hearing officer may order that any such document be made available to the respondent for inspection and copying only if the hearing officer determines that –

(i) with respect to any document withheld pursuant to paragraph (b)(1)(iii) –

(A) producing the document would not have the effect of identifying a confidential source; or

(B) the document contains material, exculpatory evidence, provided, however, that to the extent such evidence can be disclosed without disclosing the identity of a confidential source, such identity shall not be disclosed.

(ii) with respect to any document withheld pursuant to paragraph (b)(1)(iv) –

(A) the document is relevant to the subject matter of the proceeding and no good cause exists for withholding it; or

(B) the document contains material, exculpatory evidence.

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**(d) Timing of Inspection and Copying**

Unless otherwise ordered by the Board or the hearing officer, the interested division shall make documents available for inspection and copying to any respondent who is not in default under Rule 5409 no later than 14 days after the institution of proceedings pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5500, and no later than 7 days after proceedings have been instituted pursuant to Rule 5200(a)(3).

**(e) Place of Inspection and Copying**

Documents subject to inspection and copying pursuant to this Rule shall be made available to a party for inspection and copying at the Board office where they are ordinarily maintained, or at such other place as the parties, in writing, may agree. A party shall not be given custody of the documents or leave to remove the documents from the Board's offices pursuant to the requirements of this Rule other than by written agreement of the interested division. Such agreement shall specify the documents subject to the agreement, the date they shall be returned and such other terms or conditions as are appropriate to provide for the safekeeping of the documents.

**(f) Copying Costs and Procedures**

A party may obtain a photocopy of any documents made available for inspection. The party shall be responsible for the cost of photocopying. The respondent shall be given access to the documents at the Board's offices or such other place as the parties may agree during normal business hours for copying of documents at the respondent's expense.

**(g) Failure to Make Documents Available – Harmless Error**

In the event that a document required to be made available to a party pursuant to this Rule is not made available by the interested division, no rehearing or redetermination of a proceeding already heard or decided shall be required, unless the party shall establish that the failure to make the document available was not a harmless error.

Note: The interested division's obligation under this Rule relates to documents obtained by that division. Documents located only in the files of other divisions or offices are beyond the scope of the Rule, except that documents located in the



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files of other divisions and that the interested division intends to introduce as evidence shall, for purposes of this Rule, be treated as if they have been obtained by the interested division and must therefore be made available under this Rule.

### **Rule 5423. Production of Witness Statements**

#### **(a) Availability**

Upon motion by any respondent in a disciplinary proceeding, the hearing officer may order that the interested division produce for inspection and copying any statement of any person called or to be called as a witness by the division that pertains, or is expected to pertain, to his or her direct testimony and that would be required to be produced pursuant to the Jencks Act, 18 U.S.C. § 3500, if the Board were a governmental entity. Such production shall be made at a time and place fixed by the hearing officer and shall be made available to any party, provided, however, that the production shall be made under conditions intended to preserve the items to be inspected or copied.

#### **(b) Failure to Produce - Harmless Error**

In the event that a statement required to be made available for inspection and copying by a respondent is not turned over by the interested division, no rehearing or redecision of a proceeding already heard or decided shall be required unless the respondent establishes that the failure to turn over the statement was not harmless error.

#### **(c) Definition of Statement**

For purposes of this Rule, the term "statement" shall have the meaning set forth in 18 U.S.C. § 3500(e).

### **Rule 5424. Accounting Board Demands and Commission Subpoenas**

#### **(a) Accounting Board Demands and Requests**

In connection with any hearing ordered by the Board, a party may request the issuance of an accounting board demand of a registered public accounting firm or an

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associated person of such a firm, or an accounting board request of any other person. Such a demand or request may call for the attendance and testimony of a witness at the designated time and place of the hearing or for the production of documentary or other tangible evidence returnable at any designated time or place. Unless made on the record at a hearing, an application for issuance of such a demand or request shall be made in writing and served on each party. A party whose application for such a demand or request has been denied or modified may not submit any other application seeking substantially the same testimony or other evidence specified in the denied application or excluded from an otherwise granted application.

**(1) Unavailability of Hearing Officer**

In the event that the hearing officer assigned to a proceeding is unavailable, any member of the Board, or other person designated by the Board for this purpose, may grant an application for the issuance of an accounting board demand or request. A party seeking such issuance may submit the application to the Secretary, who shall direct it to a person authorized to grant the request, deny the request, or grant the request with modifications.

**(2) Signing May be Delegated**

A hearing officer may authorize issuance of an accounting board demand, or an accounting board request, and may delegate the manual signing of the demand or request to any other person.

**(3) Standards for Issuance**

Where it appears that an application for an accounting board demand or request is reasonable in scope and is reasonably calculated to encompass, or lead to the discovery of, admissible evidence, the application shall be granted. If it appears that the accounting board demand or request sought may be unreasonable, oppressive, excessive in scope, unduly burdensome, designed to seek irrelevant information, or sought for the purpose of harassment or delay, the application shall be denied. The hearing officer or other person ruling on the application may, in his or her discretion, as a condition precedent to the issuance of the demand or request, require the party seeking the demand or request to show the general relevance and reasonable scope of the testimony or other evidence sought. After consideration of all the circumstances, the hearing officer or other person ruling on the application may grant the application

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upon such conditions or with such modifications as fairness requires. In making the determination, the hearing officer or other person ruling on the application may inquire of the parties whether they will stipulate to the facts sought to be proved.

Note: Whenever possible, the parties should explore the extent to which stipulations of fact may obviate the need for issuance of accounting board demands and requests to non-parties, and the hearing officer or other person ruling on an application for issuance of an accounting board demand or request should encourage the parties to reach such stipulations when possible.

#### **(4) Witness Fees**

A witness, other than a party, who is summoned to a Board proceeding pursuant to an accounting board demand, or an accounting board request, or who is deposed pursuant to Rule 5425, shall be paid his or her reasonable expenses by the party at whose instance the witness appears.

#### **(b) Commission Subpoenas**

In connection with any hearing ordered by the Board, and upon the application of any party or on its own initiative, the Board may seek issuance by the Commission of a subpoena to any person, including any client of a registered public accounting firm, requiring the person to provide any testimony or produce any documents that the Board considers relevant or material to a Board proceeding.

### **Rule 5425. Depositions to Preserve Testimony for Hearing**

#### **(a) Procedure**

Any party desiring to take the testimony of a witness by deposition shall make a written motion setting forth the reasons why such deposition should be taken including the specific reasons why the party believes the witness will be unable to attend or testify at the hearing; the name and address of the prospective witness; the matters concerning which the prospective witness is expected to be questioned; and the proposed time and place for the taking of the deposition.

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Note: Depositions under the Rules of Board Procedure are used only to preserve testimony of a witness who would be unlikely to be able to attend the hearing. They are not permitted for purposes of discovery.

**(b) Required Finding When Ordering a Deposition**

In the discretion of the Board or the hearing officer, an order for deposition may be issued upon a finding that the prospective witness will likely give testimony material to the proceeding, that it is likely the prospective witness will be unable to attend or testify at the hearing because of age, sickness, infirmity, imprisonment or other disability, or otherwise unavailable, and that the taking of a deposition will serve the interests of justice.

**(c) Procedure at Depositions**

A witness whose testimony is taken by deposition shall be sworn or shall affirm before any questions are put to him or her. Examination and cross-examination of deponents may proceed as permitted at a hearing. The witness being deposed may have counsel present during the deposition.

**(d) Objections to Questions or Evidence**

Objections to questions or evidence shall be in short form, stating the grounds of objection relied upon. Objections to questions or evidence shall be noted in the transcript, but no person other than the hearing officer shall have the power to decide on the competency, materiality or relevance of evidence. Failure to object to questions or evidence during the deposition shall not be deemed a waiver unless the ground of the objection is one that might have been obviated or removed if presented at that time.

**(e) Filing of Depositions**

The questions propounded and all answers or objections shall be recorded or transcribed verbatim, and a transcript prepared by the deposition officer, or under his or her direction. The transcript shall be subscribed by the witness and certified by the deposition officer. The original deposition and exhibits shall be filed with the Secretary. A copy of the deposition shall be available to the deponent and each party for purchase at prescribed rates.

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**Rule 5426. Prior Sworn Statements of Witnesses in Lieu of Live Testimony**

At a hearing, any person wishing to introduce a prior, sworn statement of a nonparty witness otherwise admissible in the proceeding, in lieu of live testimony may make a motion setting forth the reasons therefor. If only part of a statement is offered in evidence, the hearing officer may require that all relevant portions of the statement be introduced. If all of a statement is offered in evidence, the hearing officer may require that portions not relevant to the proceeding be excluded. A motion to introduce a prior sworn statement in lieu of live testimony may be granted if –

- (a) the witness is dead;
- (b) the witness is out of the United States, unless it appears that the absence of the witness was procured by the party offering the prior sworn statement;
- (c) the witness is unable to attend or testify because of age, sickness, infirmity, imprisonment or other disability;
- (d) the party offering the prior sworn statement has been unable to procure the attendance of the witness by accounting board demand; or,
- (e) in the discretion of the Board or the hearing officer, it would be desirable, in the interests of justice, to allow the prior sworn statement to be used. In making this determination, due regard shall be given to the presumption that witnesses will testify orally in an open hearing. If the parties have stipulated to accept a prior sworn statement in lieu of live testimony, consideration shall also be given to the convenience of the parties in avoiding unnecessary expense.

**Rule 5427. Motion for Summary Disposition**

**(a) For Interested Division**

After a party has filed an answer and documents have been made available to that respondent for inspection and copying pursuant to Rule 5422, or after service of a motion for summary disposition by the respondent, the interested division may make a motion for summary disposition of the proceedings with respect to that respondent.

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**(b) For Respondent**

A respondent party may at any time make a motion for summary disposition of the proceeding with respect to that respondent.

**(c) Pre-motion Conference Required**

A party seeking summary disposition shall request and attend a pre-motion conference with the hearing officer before filing its motion for summary disposition.

**(1) Due-date for Filing**

At the pre-motion conference, the hearing officer will schedule a due-date for the submission of the motion for summary disposition and may, but is not required to, schedule a due-date for the submission of a response to the motion for summary judgment.

**(2) Review and Decide Procedure**

If the hearing officer has not scheduled a due-date for a response to the motion for summary judgment, upon review of the motion the hearing officer may decide to deny the motion or to require a response to the motion. A hearing officer shall not grant a motion for summary disposition until after the due-date for filing a response to the motion has passed.

**(d) Decision on Motion**

The hearing officer shall promptly grant a motion for summary disposition if the pleadings, depositions, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a disposition as a matter of law. A summary disposition, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to a sanction. A hearing officer's decision to deny a motion for summary disposition is not subject to interlocutory appeal.

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**(e) Lengths of Briefs**

Neither a brief in support of a motion for summary disposition, nor a brief in response to such a motion, shall exceed 25 pages in length, without leave of the hearing officer. Reply briefs are discouraged and are not permitted without leave of the hearing officer.

**Rules 5428. – 5439.** [Reserved]

**CONDUCT OF HEARINGS**

**Rule 5440. Record of Hearings**

**(a) Recordation**

All hearings shall be recorded and a written transcript thereof shall be prepared.

**(b) Availability of a Transcript**

Transcripts of public hearings shall be available for purchase at prescribed rates. Transcripts of nonpublic proceedings shall be available for purchase only by parties, provided, however, that any person compelled to testify at a hearing may purchase a copy of that person's own testimony.

**(c) Transcript Correction**

Prior to the filing of post-hearing briefs or other submissions, or within such earlier time as directed by the Board or the hearing officer, a party or witness may make a motion to correct the transcript. Proposed corrections of the transcript may be submitted to the hearing officer by stipulation or by motion. Upon notice to all parties to the proceeding, the hearing officer may, by order, specify corrections to the transcript.

**Rule 5441. Evidence: Admissibility**

The Board or the hearing officer may receive relevant evidence and shall exclude all evidence that is irrelevant, immaterial or unduly repetitious.

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**Rule 5442. Evidence: Objections and Offers of Proof**

**(a) Objections**

Objections to the admission or exclusion of evidence must be made on the record and shall be in short form, stating the grounds relied upon. Exceptions to any ruling thereon by the hearing officer need not be noted at the time of the ruling. Such exceptions will be deemed waived on appeal to the Board, however, unless raised –

- (1) pursuant to interlocutory review in accordance with Rule 5461;
- (2) in a proposed finding or conclusion filed pursuant to Rule 5445; or
- (3) in a petition for Board review of an initial decision filed in accordance with Rule 5460.

**(b) Offers of Proof**

Whenever evidence is excluded from the record, the party offering such evidence may make an offer of proof, which shall be included in the record. Excluded material shall be retained pursuant to Rule 5202(b).

**Rule 5443. Evidence: Presentation Under Oath or Affirmation**

A witness at a hearing for the purpose of taking evidence shall testify under oath or affirmation.

**Rule 5444. Evidence: Presentation, Rebuttal and Cross-examination**

In any proceeding, a party may present its case or defense by oral or documentary evidence, submit rebuttal evidence, and conduct such cross-examination as, in the discretion of the Board or the hearing officer, may be required for a full and true disclosure of the facts. The scope and form of evidence, rebuttal evidence, if any, and cross-examination, if any, shall be determined by the Board or the hearing officer in each proceeding.

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**Rule 5445. Post-hearing Briefs and Other Submissions**

(a) At the end of the hearing in any proceeding instituted pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5500 in which an initial decision is to be issued, the hearing officer shall, by order, after consultation with the parties, prescribe the period within which post-hearing briefs or other submissions are to be filed. Unless the hearing officer, for good cause shown, permits a different period and sets forth in the order the reasons why the different period is necessary –

(i) the party or parties directed to file first shall make its or their initial filing within 30 days of the end of the hearing; and

(ii) the total period within which all such filings and any opposition and reply submissions are to be filed shall be no longer than 90 days after the end of the hearing.

(b) In any proceeding instituted pursuant to Rule 5200(a)(3), the hearing officer may, in his or her discretion, render an initial decision without allowing for post-hearing briefs or other submissions, or may allow for such briefs or other submissions according to an expedited schedule.

**Rules 5446. – 5459. [Reserved]**

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## **APPEALS TO THE BOARD**

### **Rule 5460. Board Review of Determinations of Hearing Officers**

#### **(a) Petition for Review of Initial Decision by Hearing Officers**

Any party to a hearing may obtain Board review of an initial decision by filing a petition for review that –

(1) sets forth specific findings and conclusions of the initial decision as to which exception is taken, together with the supporting reasons for each exception; and

(2) is filed –

(i) in a proceeding instituted pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5500, within 30 days after service of the initial decision on the petitioner or within 10 days after the filing of a petition for review by another party, whichever is later; or

(ii) in a proceeding instituted pursuant to Rule 5200(a)(3), within 10 days after service of the initial decision on the petitioner.

#### **(b) Review on Board's Initiative**

The Board may, on its own initiative, order review of any initial decision, or a portion of any initial decision, at any time before the initial decision becomes final pursuant to Rule 5204(d).

#### **(c) De Novo Review**

Based on a petition for review, or on its own initiative, the Board may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper based on the record.

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**(d) Limitations on Matters Reviewed**

Review by the Board of an initial decision shall be limited to the issues specified in the petition for review or the issues, if any, specified in the briefing schedule order issued pursuant to Rule 5462(a). On notice to all parties, however, the Board may, at any time prior to issuance of its decision, raise and determine any other matters that it deems material, with opportunity for oral or written argument thereon by the parties.

**(e) Summary Affirmance**

The Board may summarily affirm an initial decision based upon the petition for review and any response thereto, without further briefing, if it finds that no issue raised in the petition for review warrants further consideration by the Board.

**Rule 5461. Interlocutory Review**

**(a) Availability**

The Board will not review a hearing officer's ruling prior to its consideration of the entire proceeding in the absence of extraordinary circumstances. The Board may decline to consider a ruling certified by a hearing officer pursuant to paragraph (c) of this Rule if it determines that interlocutory review is not warranted or appropriate under the circumstances. The Board may, at any time, on its own motion, direct that any matter be submitted to it for review.

**(b) Certification Process**

A ruling submitted to the Board for interlocutory review shall be certified in writing by the hearing officer as appropriate for interlocutory review and shall specify the basis for certification. The hearing officer shall certify a ruling only if –

- (1) the ruling would compel testimony of Board members, officers or employees or the production of documentary evidence in their custody; or

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(2) upon application by a party, within five days of the hearing officer's ruling, the hearing officer is of the opinion that –

(i) the ruling involves a controlling question of law as to which there is substantial ground for difference of opinion; and

(ii) an immediate review of the order may materially advance the completion of the proceeding.

**(c) Proceedings Not Stayed**

The filing of an application for interlocutory review or the grant of interlocutory review shall not stay proceedings before the hearing officer unless he or she, or the Board, shall so order. The Board will not consider the motion for a stay unless the motion has first been made to the hearing officer.

**Rule 5462. Briefs Filed with the Board**

**(a) Briefing Schedule Order**

Upon a timely and valid petition for review, or upon its own timely motion to review an initial decision, other than review ordered pursuant to Rule 5469, the Board shall issue a briefing schedule order directing the parties to file opening briefs and specifying particular issues, if any, as to which briefing should be limited or directed. Unless otherwise provided, opening briefs shall be filed within 40 days of the date of the briefing schedule order. Opposition briefs shall be filed within 30 days after the date opening briefs are due. Reply briefs may be filed within 14 days after the date opposition briefs are due. No briefs in addition to those specified in the briefing schedule order may be filed except with leave of the Board. The briefing schedule order shall be issued –

(1) at the time the Board orders review on its own initiative pursuant to Rule 5460(b), or orders interlocutory review on its own motion pursuant to Rule 5460; or

(2) within 21 days, or such longer time as provided by the Board, after –

(i) the last day permitted for filing a petition for review pursuant to Rule 5204(d);

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(ii) certification of a ruling for interlocutory review pursuant to Rule 5461(b).

**(b) Contents of Briefs**

Briefs shall be confined to the particular matters at issue. Each exception to the findings or conclusions being reviewed shall be stated succinctly. Exceptions shall be supported by citation to the relevant portions of the record, including references to the specific pages relied upon, and by concise argument including citation of such statutes, decisions and other authorities as may be relevant. If the exception relates to the admission or exclusion of evidence, the substance of the evidence admitted or excluded shall be set forth in the brief, in an appendix thereto, or by citation to the record. Reply briefs shall be confined to matters in opposition briefs of other parties.

**(c) Length Limitation**

Opening and opposition briefs shall not exceed 30 pages and reply briefs shall not exceed 15 pages, exclusive of pages containing the table of contents, table of authorities, and any addendum, except with leave of the Board.

**Rule 5463. Oral Argument Before the Board**

**(a) Availability**

The Board, on its own motion or the motion of a party, may order oral argument with respect to any matter. Motions for oral argument with respect to whether to affirm all or part of an initial decision by a hearing officer shall be granted unless exceptional circumstances make oral argument impractical or inadvisable. The Board will consider appeals, motions and other matters properly before it on the basis of the papers filed by the parties without oral argument unless the Board determines that the presentation of facts and legal arguments in the briefs and record and the decisional process would be significantly aided by oral argument.

**(b) Procedure**

Requests for oral argument shall be made by separate motion accompanying the initial brief on the merits. The Board shall issue an order as to whether oral argument is

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to be heard, and if so, the time and place therefor. The grant or denial of a motion for oral argument shall be made promptly after the filing of the last brief called for by the briefing schedule. If oral argument is granted, the time fixed for oral argument shall be changed only by written order of the Board, for good cause shown. The order shall state at whose request the change is made and the reasons for any such change.

**(c) Time Allowed**

Unless the Board orders otherwise, not more than one half-hour per side will be allowed for oral argument. The Board may, in its discretion, determine that several persons have a common interest, and that the interests represented will be considered a single side for purposes of allotting time for oral argument. Time will be divided equally among persons on a single side, provided, however, that by mutual agreement they may reallocate their time among themselves. A request for additional time must be made by motion filed reasonably in advance of the date fixed for argument.

Note: The term "side" is used in this Rule to indicate that the time allowed is afforded to opposing interests rather than to individual parties. If multiple parties have a common interest, they may constitute only a single side.

**(d) Participation of Board Members**

A member of the Board who was not present at the oral argument may participate in the decision of the proceeding, provided that the member has reviewed the transcript of such argument prior to such participation. The decision shall state whether the required review was made.

**Rule 5464. Additional Evidence**

Upon its own motion or the motion of a party, the Board may allow the submission of additional evidence. A party may file a motion for leave to adduce additional evidence at any time prior to issuance of a decision by the Board. Such motion shall show with particularity that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence previously. Any other party may file a response to the motion within 5 days after the motion is filed, or such longer time as the Board may allow. The Board may accept or hear additional evidence, or it may remand or refer the proceeding to a hearing officer for the taking of additional evidence, as appropriate.

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**Rule 5465. Record Before the Board**

The Board shall determine each matter on the basis of the record.

**(a) Contents of the Record**

In proceedings for final decision before the Board, the record shall consist of –

- (1) all items part of the hearing record below in accordance with Rule 5202(a);
- (2) any petitions for review, cross-petitions or oppositions; and
- (3) all briefs, motions, submissions and other papers filed on appeal or review.

**(b) Transmittal of Record to Board**

Within 14 days after the last date set for filing briefs or such later date as the Board directs, the Secretary shall transmit the record to the Board.

**(c) Review of Documents Not Admitted**

Any document offered in evidence but excluded by the hearing officer or the Board and any document marked for identification but not offered as an exhibit shall not be considered a part of the record before the Board on appeal but shall be transmitted to the Board by the Secretary if so requested by the Board. In the event that the Board does not request the document, the Secretary shall retain the document not admitted into the record until the later of –

- (1) the date upon which the Board's order becomes final, or
- (2) the conclusion of any Commission and judicial review of that order.

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**Rule 5466. Reconsideration**

**(a) Scope of Rule**

A party may file a motion for reconsideration of a final order issued by the Board.

**(b) Procedure**

A motion for reconsideration shall be filed within 10 days after service of the order complained of on each party, or within such time as the Board may prescribe upon motion of the person seeking reconsideration, if made within the foregoing 10-day period. The motion for reconsideration shall briefly and specifically state the matters of record alleged to have been erroneously decided, the grounds relied upon, and the relief sought. Except with permission of the Board, a motion for reconsideration shall not exceed 15 pages. No responses to a motion for reconsideration shall be filed unless requested by the Board.

**Rule 5467. Receipt of Petitions for Commission or Judicial Review**

A registered public accounting firm –

(a) that has filed a petition for Commission review of a final disciplinary sanction of the Board pursuant to Section 19(d)(2) of the Exchange Act, or a petition for court review of a Commission order with respect to such a sanction pursuant to Section 25(a)(1) of the Exchange Act, or

(b) that is associated with a person, other than a person primarily associated with another registered public accounting firm, who has filed such a petition,

shall file a notice and copy of the petition with the Secretary within 10 days after the petition is made.

Note: Appeals of final disciplinary sanctions by the Board are instituted by the filing of a petition for review in accordance with the Commission's Rules of Practice. Unless directed otherwise by statute, appeals of Commission orders and decisions on a sanction imposed by the Board to a court of appeals are instituted by the filing of a petition for review in accordance with the Federal Rules of Appellate Procedure. See Fed. R. App. P. 15(a).

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**Rule 5468. Appeal of Actions Made Pursuant to Delegated Authority**

**(a) Notice of Intention to Petition for Review**

A person intending to seek Board review of an action made pursuant to delegated authority shall file a written notice of intention to petition for review within five days after actual notice to the petitioner of the action or service of notice of the action, whichever is earlier. The notice shall identify the petitioner and the action complained of, and shall be accompanied by a notice of appearance pursuant to Rule 5401(c). The Board will allow late filing of a notice of intention to petition for review upon a showing that a delay in service, through no fault of the petitioner's, made compliance with the time limit set forth in this paragraph impossible or unreasonably burdensome.

**(b) Petition for Review**

Within five days after the filing of a notice of intention to petition for review pursuant to paragraph (a) of this Rule, the person seeking review shall file a petition for review containing a clear and concise statement of the issues to be reviewed and the reasons why review is appropriate. The petition shall include exceptions to any findings of fact or conclusions of law made, together with supporting reasons for such exceptions based on appropriate citations to such record as may exist. These reasons may be stated in summary form. The Board will review all actions made pursuant to delegated authority with respect to which timely notices of intention to petition for review, and timely petitions for review, have been filed.

**Rule 5469. Board Consideration of Actions Made Pursuant to Delegated Authority**

**(a) Board Review**

Upon a petition for review, or upon its own initiative, the Board may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, any action made pursuant to delegated authority. The Board may, in its discretion, act summarily on the basis of the petition, act on the basis of the petition and any written response provided by the staff and served on the petitioner, or request the submission of additional statements in support of or in opposition to the petition.

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**(b) No Stay of Effect of Delegated Action**

An action made pursuant to delegated authority shall have immediate effect and be deemed the action of the Board. The effect of any action made pursuant to delegated authority shall not be stayed, and no petition for review shall operate as a stay, unless otherwise ordered by the Board.

**Rules 5470. – 5499. [Reserved]**

**Part 5 – Hearings on Disapproval of Registration Applications**

**Rule 5500. Commencement of Hearing on Disapproval of a Registration Application**

The Board may commence a proceeding to determine whether to approve or disapprove a public accounting firm's application for registration when, based on review of an application for registration as a registered public accounting firm –

(a) the Board determines, pursuant to Rule 2106(b)(2)(ii), to provide the applicant with written notice of a hearing to determine whether to approve or disapprove the application; and

(b) within such period, as the Board permits, after the date of service of a notice of a hearing whether to approve or disapprove an application for registration pursuant to Rule 2106(b)(2)(ii), the public accounting firm served with such notice files with the Secretary a written request for a hearing date and a notice of appearance pursuant to Rule 5401(c), and includes with the request –

(1) a statement that the public accounting firm has elected not to treat the notice as a written notice of disapproval for purposes of Section 102(c) of the Act; and

(2) a statement describing with specificity why the public accounting firm believes that the Board should not issue a written notice of disapproval.



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**Rule 5501. Procedures for a Hearing on Disapproval of a Registration Application**

Proceedings instituted pursuant to Rule 5500 shall be subject to procedures as described in Parts 2 and 4 of Section 5 of the Board's Rules.

**Appendix 2 – Section-by-Section Analysis of  
Rules Relating to Investigations and Adjudications**

The Board has adopted 64 rules relating to investigations and adjudications along with definitions that will appear in Rule 1001 and a general rule on time computation as Rule 1002. Each of the rules and definitions is discussed below.

**Rule 1001 – Definitions of Terms Employed in Rules**

Rule 1001 contains definitions of terms used in the Board's rules. The rules relating to investigations and adjudications employ certain terms that the Board is adding to the terms defined in Rule 1001.

*Accounting Board Demand*

Rule 1001(a)(ix) defines "accounting board demand" as a command to produce documents and/or to appear at a certain time and place to give testimony. The rules use this term only to identify demands made upon registered public accounting firms and associated persons of such firms. Under the Act, the Board has authority to require those firms and persons to provide any testimony or documents sought by the Board in furtherance of its responsibilities under the Act, and including in particular any testimony or documents that the Board considers relevant to an investigation.

*Accounting Board Request*

Rule 1001(a)(x) defines "accounting board request" as a request to produce documents and/or to appear at a certain time and place to give testimony. The rules use this term to distinguish the Board's efforts to obtain documents and testimony from

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persons other than registered public accounting firms and their associated persons.

*Bar*

Rule 1001(b)(ii) defines "bar" as a permanent disciplinary sanction prohibiting a person from being associated with a registered public accounting firm. The rules distinguish between the concepts of "bar" and "suspension." Both sanctions, when applied to an associated person, prohibit the person from being an associated person of a registered public accounting firm. A suspension, however, as defined below, is a time-limited sanction that expires at a fixed time after which the person may resume being an associated person without any other action by the person or the Board. In contrast, a bar is a permanent sanction that does not expire unless the person petitions the Board for termination of the bar, pursuant to the provisions of the rules, and the Board grants the petition. In some cases, the Board may impose a bar that expressly provides that a person may petition for termination of the bar after a fixed period. In other cases, the Board may impose a bar with no such provision.

*Counsel*

Proposed Rule 1001(c)(ii) defined "counsel" as an attorney at law admitted to practice before the Supreme Court of the United States or the highest court of any state. One commenter suggested that the Board add a "good standing" requirement to the definition, and we have incorporated that suggestion in the final rule. The commenter

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also suggested that we revise the definition to encompass persons admitted to practice in any state "or province" of the United States. We have not incorporated that suggestion. The definition of "counsel" uses the term "state," which both Section 2(a)(16) of the Act and rule 1001(s)(iii) separately define to include the District of Columbia, Puerto Rico, the Virgin Islands, and any other territory or possession of the United States.

*Disciplinary Proceeding*

Rule 1001(d)(i) defines "disciplinary proceeding" as a proceeding initiated by an order instituting proceedings, held for the purpose of determining whether a registered public accounting firm, or any person associated with a registered public accounting firm (1) has engaged in any act or practice, or omitted to act, in violation 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 Securities and Exchange Commission (the "Commission") issued under the Act, or professional standards; or (2) has failed reasonably to supervise an associated person in connection with any such violation by that person; or (3) or has failed to cooperate with the Board in connection with an investigation; and (4) whether to impose a sanction pursuant to Rule 5300. The provision concerning failure to supervise has been added to the final rule to make the

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rule consistent with 5200(a) concerning the grounds for commencing disciplinary proceedings.

Some commenters expressed concern about the relationship between the prospect of Board discipline for violations of "professional standards" and the Board's definition of "professional standards" as set out in proposed rule 1001(d)(i) as part of the Board's proposing release concerning inspection rules. These commenters stated that because "professional standards" is defined to include accounting principles, the Board's proposed framework creates the specter of auditor liability for the audit client's violation of generally accepted accounting principles ("GAAP").

We have not changed the proposal. Both the definition of "professional standards" and the Board's responsibility to discipline auditors for violations of professional standards come directly from the Act. We note, however, that we do not read these provisions to expand the scope of the liability that an auditor may face with respect to an issuer's failure to comply with GAAP, beyond the scope that existed at the time the Act became law.

*Document*

Rule 1001(d)(ii) defines "document" as synonymous in meaning and equal in scope to its usage in Federal Rule of Civil Procedure 34(a), including, without limitation, electronic or computerized data compilations. A draft or non-identical copy is a



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separate document within the meaning of this term. In no event shall the term "document" be construed to be limited to auditwork papers.

*Hearing Officer*

Rule 1001(h)(i) defines "hearing officer." The Board proposed a definition that included a panel of Board members constituting less than a quorum of the Board, an individual Board member, or any other person duly authorized by the Board to preside at a hearing. Several commenters expressed the view that neither Board members nor staff of the interested division should ever serve as hearing officers. We never intended to permit staff of the interested division to serve as hearing officers, and we have revised the rule to exclude that possibility. Nor did we intend to provide for a Board member to serve as a hearing officer except in an extraordinary situation, and we are now persuaded that the rule should exclude that possibility as well. In general, we intend to rely on a corps of qualified persons whose service to the Board is strictly limited to the role of hearing officer. We may rely on consultants for this purpose, or we may employ a staff of hearing officers, or we may rely on a combination of the two.

Although we exclude the possibility of a Board member serving as a hearing officer, we do not agree with all of the reasons suggested by commenters for doing so. In particular, we reject the suggestion that there is any unfairness or conflict of interest in the prospect of a Board member participating in the decision to initiate an



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investigation or disciplinary proceeding and then serving as a hearing officer in that matter. Even among federal agencies subject to the Administrative Procedure Act (to which the Board is not subject) such a practice is well-established as comporting with fair procedural principles.

One commenter suggested that the rule should require a hearing officer to demonstrate a lack of bias on each matter. The comment seems premised on the notion that a hearing officer should be presumed to be biased unless he or she demonstrates otherwise. We decline to adopt that presumption. We expect that hearing officers will be unbiased and that they will take appropriate steps in situations in which their impartiality might fairly be questioned. In addition, the rules provide an opportunity for a party to show why a hearing officer should be recused.

#### *Interested Division*

Rule 1001(i)(iv) defines "interested division" as a division or office of the Board assigned primary responsibility by the Board to participate in a particular proceeding. As a general matter, the interested division in a disciplinary proceeding will be the Division of Enforcement and Investigations, and the interested division in a hearing on disapproval of a registration application will be the Division of Registration and Inspections. The definition is adapted from Rule 101(a)(6) of the Commission's Rules of Practice.



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*Order Instituting Proceedings*

Rule 1001(o)(ii) defines "order instituting proceedings" as an order issued by the Board commencing a disciplinary proceeding.

*Party*

Rule 1001(p)(iii) defines "party" as the interested division, any person named as a respondent in an order instituting proceedings or notice of a hearing, any applicant named in the caption of any order, or any person seeking Board review of a decision.

*Person*

Rule 1001(p)(iv) defines "person" as any natural person or any business, legal or governmental entity or association.

*Revocation*

Rule 1001(r)(iii) defines "revocation" as a permanent disciplinary sanction terminating a firm's registration. The rules distinguish between the concepts of "revocation" and "suspension." Both sanctions, when applied to a firm, prohibit the firm from preparing or issuing, or participating in the preparation or issuance of, audit reports. A suspension, however, as defined below, is a time-limited sanction that expires at a fixed time after which the firm may resume such work without any other action by the firm or the Board. In contrast, revocation is a permanent sanction that does not expire unless the firm, with the Board's permission, reapplies for registration

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pursuant to the provisions of the rules, and the Board approves the application. In some cases, the Board may impose a revocation that expressly provides that a firm may reapply for registration after a fixed period. In other cases, the Board may impose a revocation with no such provision.

*Secretary*

Rule 1001(s)(iii) defines "Secretary" as the Secretary of the Board.

*Suspension*

Rule 1001(s)(iv) defines "suspension" as a temporary disciplinary sanction which lapses by its own terms and prohibits (1) a registered public accounting firm from preparing or issuing, or participating in the preparation or issuance of, any audit report with respect to any issuer; or (2) a person from being associated with a registered public accounting firm. A suspension is distinct from a bar (as to an associated person) and a revocation (as to a firm) in that a suspension is a sanction that expires by its own terms at a fixed time, with no further action required of the associated person, the firm, or the Board.

**Rule 1002 – Time Computation**

Rule 1002 describes the method by which the Board shall compute time for purposes of complying with deadlines in the Board's rules. We proposed this rule as rule 5410. As such, its application was limited to the adjudication process. In response



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to comments received on our proposed rule on withdrawal from registration, we believe that it is appropriate to apply the substance of the time computation rule more generally to the Board's processes. We have adopted it as a part of our general rules, with minor technical changes.

### **Rule 5000 – General**

Rule 5000 requires that registered public accounting firms and any associated persons of such firms comply with all Board orders to which they are subject. The Act authorizes the Board to take certain action with respect to, or require certain things of, registered public accounting firms and their associated persons. For example, the Act authorizes the Board to require such firms and persons to produce documents or to provide testimony, and the Act authorizes the Board to impose significant disciplinary sanctions on such firms and persons for various violations and for noncooperation with Board investigations. In exercising its authority, the Board will frequently act through the vehicle of a Board order. A requirement of compliance with such orders is implicit in the authority to take the action, and Rule 5000 makes that requirement explicit.

#### **Part 1 – Inquiries and Investigations**

Part 1 of the Board's Rules on Investigations and Adjudications consists of Rules 5100 through 5112. These rules address procedural matters concerning the conduct of informal inquiries by Board staff and formal Board investigations.

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### **Rule 5100 – Informal Inquiries**

The Board contemplates that the staff of the Division of Enforcement and Investigations will sometimes conduct informal inquiries to determine whether to recommend that the Board open a formal investigation on a matter. Rule 5100 describes generally the circumstances in which the staff may conduct an informal inquiry (Rule 5100(a)) and the scope of the activity in which the staff may engage in an informal inquiry (Rule 5100(b)).

Under Rule 5100(a), the staff may undertake an informal inquiry where it appears to the staff that an act or practice, or an omission to act, by a registered public accounting firm or an associated person may violate the Act, the Board's rules, 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. Under Rule 5100(b), the staff may pursue an informal inquiry by requesting documents, information, or testimony from any person. The staff may not, in an informal inquiry, issue accounting board demands.

One commenter suggested that the Board should be required to close an informal inquiry within a specified period of time. Another commented that the rule should include a note that would exhort the staff to begin informal inquiries with the

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narrowest possible request for information, rather than broad requests for all relevant documents. We have adopted the rule as proposed, rather than with the suggested modifications.

These comments, like a number of comments made with respect to many of the proposed rules, seem premised on a concern that the Board and its staff might not always act reasonably unless Board rules expressly require all steps that might be reasonable and expressly prohibit unreasonableness. We do not accept this premise and, as a general matter, we have not adopted commenters' suggestions along these lines. In adopting this set of rules, we proceed from the premise that both the Board and the staff will act reasonably, and that it is generally not the role of these rules to define what is reasonable for all circumstances.

With respect to the particular comments on this rule, we expect that the staff will not keep informal inquiries open beyond the time reasonably necessary to determine whether a formal investigation is warranted, and we expect the staff to seek and review any documents relevant to making that determination. If we perceive over time that the staff's exercise of its discretion develops into practices that impose unreasonable burdens or that needlessly prolong uncertainty, we can take corrective steps.

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**Rule 5101 – Commencement and Closure of Investigations**

Rule 5101 describes generally the processes by which the Board will commence and close formal investigations. The Board may commence a formal investigation when it appears that an act or practice, or omission to act, by a registered public accounting firm or any person associated with such a firm 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 issued under the Act, or professional standards. Rule 5101(a)(1) provides that the way the Board will commence an investigation is by issuing an order of formal investigation. Rule 5101(a)(2) provides that the Board may, in the formal order, designate Board staff members, or groups of staff members (such as a particular division or office) authorized to issue accounting board demands and otherwise require or request the cooperation of any person in connection with the investigation. Rule 5101(b) provides that the Board may issue an order suspending a formal investigation for a specified period of time or terminating a formal investigation.

Some commenters suggested that the rules should provide that firms and associated persons would receive prompt notice of the commencement of an investigation concerning them. We decline to adopt this suggestion. Notice of the

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onset of an investigation may, in many situations, be inconsistent with a sound approach to conducting the investigation. The absence of a notice requirement is common in other investigative contexts that are generally analogous to the Board's processes (such as Commission investigations and NASD investigations), and we perceive no unfairness in declining to provide notice.

Moreover, the persons whose conduct might provide the original reason for the investigation may not be the persons (or may not be the only persons) as to whom the staff recommends enforcement action at the conclusion of the investigation. Identifying the investigative evidentiary threshold that would somehow trigger an obligation to provide notice to a new person would be unworkable as a practical matter. It would also give rise to unproductive peripheral disputes about whether notice was unfairly delayed or withheld while the staff obtained documents or information from the person. In the context of a Board investigation, a person's rights do not vary depending on whether the person is in some sense a subject of the investigation. A registered firm and an associated person have the same rights and the same obligation to cooperate either way. Notice would serve no purpose that relates to either the efficiency or the fairness of the investigation, and a notice requirement would serve no purpose other than to generate peripheral points of dispute.

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One commenter also noted that Commission practices permit a person to petition for the closing of an investigation. The rules we have adopted do not provide a procedure for such a practice but, as we understand it, neither do Commission rules. Nothing in our rules prevents the development of a practice by which persons might request the closing of an investigation, and the Board and its staff will consider such requests.

**Rule 5102 – Testimony of Registered Public Accounting Firms and Associated Persons in Investigations**

Section 105(b)(2)(A) of the Act authorizes the Board to promulgate rules requiring the testimony of any registered public accounting firm or any associated person of such a firm with respect to any matter that the Board considers relevant or material to an investigation. Rule 5102(a) implements that authority by providing that the Board and the staff of the Board designated in the order of formal investigation may require such testimony. Paragraphs (b) through (e) of Rule 5102 describe procedures related to obtaining and recording that testimony.

Two comments addressed the scope of Rule 5102(a), although from slightly different perspectives. One commenter expressed concern that the breadth of the rule might allow the Board to seek testimony from a firm's general counsel. This commenter suggested the Commission has a practice of not seeking testimony from a firm's general counsel and urged that we follow the Commission's example. Another commenter

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suggested adding a "reasonableness" standard so that the Board cannot embark on "fishing expeditions."

We have adopted the rule as proposed. The scope of permissible testimony demands reflected in the rule is the scope provided by the Act, and we decline to narrow it. The standard is broad enough to allow the Board to seek information that a firm's general counsel may have, although, as discussed below in connection with Rule 5106, we do not intend to invade the attorney-client privilege. Again, we anticipate that the staff's practices in this regard will be reasonable, and we decline to adopt a rule based on a contrary premise.

Rule 5102(b) provides that the Board or staff shall require testimony by serving an accounting board demand. Under the rule, the demand must give reasonable notice of the time and place for taking testimony, must describe the methods by which the testimony will be recorded, and, if the demand is directed to a firm rather than to a natural person, must supply a description with reasonable particularity of the matters on which examination is requested.

The rule does not impose any minimum period of notice for testimony, but does require reasonable notice. The section-by-section analysis accompanying our proposing release stated that we anticipated that the staff would, as a general matter, provide at least five business days notice. Several commenters interpreted that as an

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indication that five days would be the norm, regardless of the nature of the matter in which testimony is sought. Commenters suggested that the rule should prescribe a specific period of notice, much longer than five days. Suggestions included 14 days, 15 days, and 21 days. We decline to codify a particular period of notice, because there will be circumstances in which there is no compelling reason why 21, or even 14, days notice is necessary, and there may be legitimate reasons for requiring the testimony sooner. We also anticipate, however, that it will not be unusual for the staff to provide two to three weeks notice. We reiterate our premise that Board staff will act fairly and reasonably, and we emphasize that we expect firms and associated persons to cooperate with requirements that are reasonable under the circumstances. We will enforce that expectation through disciplinary proceedings for noncooperation where appropriate.

One commenter also suggested that Rule 5102(b)(3)'s requirement to provide a description of the matters on which examination is requested should be broadened to apply to demands made to individuals as well as to firms. We decline to adopt the suggestion. The requirement to provide a description to a firm is based on Rule 30(b)(6) of the Federal Rules of Civil Procedure, which requires a description when seeking the testimony of an entity, so that the entity may supply the appropriately knowledgeable individuals to testify on its behalf, and may take steps to ensure that the

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individuals have the right information. No similar rationale applies when seeking testimony from an individual. An individual should be prepared to testify from his or her personal knowledge with respect to whatever questions the staff has that are relevant to the investigation.

Rule 5102(c) describes procedures related to the actual conduct of the examination. Rule 5102(c)(1) provides that each witness shall be required to declare that the witness will testify truthfully, by oath or affirmation. The oath or affirmation provision of the rule is adapted from Federal Rule of Evidence 603. The authority to administer and obtain such an oath or affirmation is implicit in the Board's authority to require testimony.

Rule 5102(c)(2) provides that examinations shall be conducted before a reporter designated by the Board's staff to record the examination. Rule 5102(c)(3) imposes restrictions on who may be present during the examination. Persons who may be present are limited to the witness, the witness's counsel (subject to Rule 5109(b), discussed below), any member of the Board or the Board's staff, the reporter, and any other person whom the Board or the staff designated in the order of formal investigation determine to be appropriate permit to be present. All of these provisions, however, are qualified by the restriction that in no event shall any person (other than the witness) who has been or is reasonably likely to be examined in the investigation be present. This

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last restriction is not limited to registered public accounting firms and associated persons of such firms but also includes any other person from whom the Board or the staff could seek to require testimony pursuant to a Commission subpoena (as described in Rule 5111).

Several commenters suggested that the rules should allow a witness and his or her counsel to be accompanied by a technical expert consultant during testimony as a matter of right. Commenters stated that allowing accounting consultants helps to ensure that a witness's rights are fully protected and helps to produce a better investigative record. Commenters also cited a district court opinion, S.E.C. v. Whitman, 613 F.Supp. 48 (D.D.C 1985) (requiring the Commission to permit an expert consultant to assist counsel during investigative testimony) as authority for the proposition that the Board should allow for the presence of such consultants.

We adopt the rule that we proposed, without modification. The rule provides sufficient flexibility for the staff to permit a technical consultant to be present during investigative testimony, and we expect the staff to allow that presence in appropriate circumstances and on appropriate terms, including, for example, that the consultant not be a partner or employee of the firm with which the witness is associated. We expect the staff to be accommodating, but we also expect the staff to be vigilant about not

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permitting a firm's internal personnel effectively to monitor an investigation by sitting in on testimony of all firm personnel.<sup>1/</sup>

Commenters also stated that the rule should explicitly provide that the counsel representing a witness may also represent an accounting firm with which the witness is associated. One commenter went further, suggesting that even if a witness retains outside counsel, the firm's in-house counsel should also be permitted to attend the testimony.

The rule allows counsel to represent a witness and the witness's firm to the extent that such dual representation is consistent with counsel's ethical obligations generally. The rule does not allow for the presence of a firm's in-house counsel, or any other counsel, who does enter a notice of appearance affirmatively stating that he or she represents the witness. Counsel who represents both the firm and the witness, and who, during testimony, becomes aware of a conflict that would cause him or her to cease representing the witness, may not continue to be present.

Rule 5102(c)(4) is modeled on Rule 30(b)(6) of the Federal Rules of Civil Procedure. Rule 5102(c)(4) provides that a registered public accounting firm that is required to provide testimony shall designate one or more persons to testify on its

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<sup>1/</sup> Whatever binding precedential value Whitman may have in the context of a Commission investigation, it has none in the context of a Board investigation. The Whitman decision rests on the requirements of the Administrative Procedure Act, which is not applicable to Board proceedings.

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behalf and may set forth, for each person designated, the matters on which the person will testify. Those persons are then required to testify as to matters known or reasonably available to the firm.

One commenter suggested that Rule 30(b)(6) does not provide an appropriate model for a corresponding procedure in a Board investigation because the Federal Rules of Civil Procedure govern a different type of proceeding. The commenter suggested that the scope of testimony that may be requested through this procedure should be more limited than under the Federal Rules. The commenter also noted that the proposed rules lack a procedure to allow the examinee to supplement examination answers at a later time.

We have not modified the rule in response to those comments. The Act provides the relevant scope of testimony that we may obtain from a registered firm. Rule 5102(c)(4) affords a firm flexibility with respect to the person or persons through whom it supplies that testimony. The rules do provide a procedure for reviewing and requesting changes to a transcript, as described below. The rules do not provide a procedure for otherwise supplementing testimony because any supplementation should be accomplished through additional examination under oath rather than through a supplemental written document. If a firm believes such supplementation is necessary, it

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may contact the staff, and the staff may decide whether to resume the examination of a designated individual.

We have made technical changes to rule 5102(c)(4). Specifically, we have substituted the word "individual" for "person" where appropriate to avoid confusion that could flow from the fact that "person" is defined to include an entity.

Rule 5102(e) allows a witness a period of time, after being notified that the transcript or other recording of the examination is available for review, to describe any changes in form or substance that the witness would make and to supply the reasons for such changes. Under the rule, the transcript shall be accompanied by the reporter's certification that the witness was duly sworn and that the transcript is a true record of the testimony, and shall indicate whether the witness requested to review the transcript. The reporter shall also append to the transcript any changes to the testimony made by the witness during the review period described above.

Proposed Rule 5102(e) allowed a witness 10 days to request changes to the transcript. One commenter suggested that the period for requesting changes to a transcript should be 30 days. We have not adopted that suggestion, but we have modified the rule to provide for 15 days and to allow for an extension of the 15-day period with the approval of the Director of the Division of Enforcement and Investigations.

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**Rule 5103 – Demands for Production of Audit Workpapers and Other Documents in Investigations from Registered Public Accounting Firms and Associated Persons**

Section 105(b)(2)(B) of the Act authorizes the Board to promulgate rules requiring the production of audit workpapers and any other document or information in the possession of any registered public accounting firm or any associated person of such a firm, wherever domiciled, with respect to any matter that the Board considers relevant or material to an investigation. Rule 5103(a) implements that authority by providing that the Board and the staff of the Board designated in the order of formal investigation may require production of such documents and information.

One commenter suggested that we change the caption of the rule to describe more precisely the subject of the rule. We have not adopted the specific caption suggested, but we have followed the suggestion generally by changing the caption from "Production of Audit Workpapers and Other Documents in Investigations" to the caption above.

One commenter suggested that these rules should define "audit workpapers." The commenter made suggestions about what the definition should include. We understand those comments to address document retention issues rather than rules on investigations. We will address audit documentation and document retention issues in the context of our establishment of auditing and related professional practice standards.



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We emphasize, however, that the scope of our authority to demand documents goes well beyond documents that might be considered "audit workpapers," and includes any document that may be relevant or material to consideration of whether there have been violations of the Act, our rules, 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.

Another commenter stated that the standard was subjective in nature and suggested that the rule should include a "reasonableness" requirement. We decline to include that requirement in the rule. The scope of, and standard for, Board document demands is set out in the Act, and we intend for the rule to incorporate the full scope of our authority to demand documents.

A commenter also suggested that the rules should permit a firm to seek Board review of the scope of an accounting board demand issued by the staff. The commenter suggested that firms and associated persons should be able to ask that the Board quash an accounting board demand or issue a protective order limiting the scope of the demand. Finally, the commenter suggested that a firm or associated person should be able to seek review of a Board denial of such a request without having to risk a noncooperation proceeding and sanction.

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We decline to adopt these suggested additions. In essence, the commenter argues that a firm or associated person should not face a noncooperation sanction unless the firm or associated person has first had a chance to obtain Commission (and perhaps, implicitly, court of appeals) review of the appropriateness of the accounting board demand, has failed to persuade the Commission or court of the inappropriateness of the demand, and then still fails to comply with the demand.

We first address the notion of providing by rule for review of Board decisions concerning the scope of accounting board demands. The Act provides for no such review and, under the Act, we see no mechanism for a firm or associated person to present that question to the Commission or a court other than through a petition for review of a disciplinary sanction for noncooperation.<sup>2/</sup>

Nor are we persuaded of any need to provide a special mechanism to petition for Board review of an accounting board demand issued by the staff. When the staff cannot resolve disputes about the scope of a demand, we expect that the staff, where appropriate, will recommend the institution of noncooperation proceedings.

That is not to say, however, that a person proceeding reasonably and in good faith can only obtain Board review through a process that necessarily ends in a sanction

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<sup>2/</sup> This discussion concerns general challenges to the scope of an accounting board demand. We separately address disputes related to privilege assertions in our discussion of Rule 5106, below.

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if the Board sides with the staff. A noncooperation proceeding will normally include an opportunity for a person to submit a statement of position under Rule 5109(d), explaining why the Board should conclude that the demand exceeds the permissible statutory scope of documents, testimony, or information that the Board may demand. The Board will take that submission into account in determining whether to institute noncooperation proceedings.

If the submission does not persuade the Board, a noncooperation proceeding and sanction need not follow automatically. Some cases may involve a good faith assertion of a position that raises a genuine issue concerning the scope of the demand. In those cases, the Board might communicate its rejection of the person's position but also indicate that noncooperation proceedings will not be commenced if the person complies with the demand within a certain time. At that point, the person could comply or, at the risk of a sanction, could continue to contest the appropriateness of the demand in the hope of prevailing before a hearing officer, or on review by the Board, the Commission, or the court of appeals.

We should not be understood as suggesting that we will routinely afford an opportunity to cure noncompliance before authorizing noncooperation proceedings. We are not describing a process that effectively affords a no-risk mechanism for delaying compliance with every accounting board demand. We will, based on the circumstances

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of each case, determine whether it is appropriate to afford an opportunity to cure before noncooperation proceedings are instituted, or whether a noncooperation proceeding is appropriate whether or not the noncompliance is cured. We may, for example, determine that the circumstances warrant a hearing on noncooperation and the possible imposition of a sanction even if the noncompliance is cured, while always holding out the possibility that curing the noncompliance may bear on the ultimate severity of any sanction.

Rule 5103(b) provides that an accounting board demand for documents or information shall set forth a reasonable time and place for such production. Rule 5103(b) does not impose any minimum notice requirement before production shall be due. The section-by-section analysis accompanying our proposing release stated that we anticipated that the staff would, as a general matter, provide at least five business days notice. Several commenters interpreted that as an indication that five days would be the norm, regardless of the nature and volume of documents demanded. Commenters suggested that the rule should prescribe a specific period of notice, much longer than five days. Suggestions included 14 days, 21 days, and 30 days. We decline to codify a particular period of notice, because there will be circumstances in which there is no compelling reason why 30, or even 14, days notice is necessary and there may be legitimate reasons for requiring the documents sooner. We also

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anticipate, however, that it will not be unusual for the staff to provide two to three weeks notice. We reiterate our premise that Board staff will act fairly and reasonably, and we again emphasize that we expect firms and associated persons to cooperate with requirements that are reasonable under the circumstances. We will enforce that expectation through disciplinary proceedings for noncooperation where appropriate.

Proposed Rule 5103(b) provided that unless otherwise requested or permitted in the accounting board demand, the documents produced shall be the originals, and any document that exists in electronic form shall be produced in electronic form. Commenters stated that production of original documents, including workpapers, can be disruptive to ongoing audit engagements and suggested that the rule provide for production of copies rather than originals. To accommodate this concern, we have modified the rule to permit production of copies unless otherwise specified in the accounting board demand. The rule also requires, however, that the originals be maintained in a reasonably accessible manner, be readily available for inspection by the staff, and not be destroyed without the staff's consent. An original document that could otherwise be destroyed consistent with any applicable document retention requirements or other legal requirements may nevertheless not be destroyed without the staff's consent if it is responsive to an accounting board demand received by the firm.

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We have made technical changes to rule 5102(c)(4). Specifically, we have substituted the word "individual" for "person" where appropriate to avoid confusion that could flow from the fact that "person" is defined to include an entity.

**Rule 5104 – Examination of Books and Records in Aid of Investigations**

Section 105(b)(2)(B) of the Act authorizes the Board to promulgate rules allowing the Board to inspect the books and records of a registered public accounting firm or any associated person of such a firm, wherever domiciled, to verify the accuracy of any documents and information supplied by the firm or person in an investigation. Rule 5104 implements that authority by providing that the Board and the staff designated in an order of formal investigation may examine such books and records to verify the accuracy of any documents or information supplied in the course of an informal inquiry or formal investigation. Any such examination would be separate and apart from any Board inspection pursuant to Section 104 of the Act and the Board's rules thereunder and would not be subject to the provisions of Section 104 or the Board's rules thereunder. Rule 5104 requires that the firm or person allow such examination upon demand, and does not provide for any minimum notice period.

One commenter suggested that a Rule 5104 examination should only occur with prior express Board approval. We have not adopted that specific suggestion, but we agree that a firm should not be subject to a Rule 5104 examination at the behest of

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every staff member. We have modified the rule to provide that any such examination requires the prior approval of the Director of Enforcement and Investigations.

Commenters also expressed concern that the Rule 5104 procedure did not seem to allow a firm an opportunity to assert appropriate privileges as to the information to be examined. We expect the staff to apply the rule such that a firm that acts diligently will have an opportunity to make any valid privilege assertions before examination. Accordingly, we have revised Rule 5106, discussed below, to reflect the possibility of privilege assertions in the context of a Rule 5104 examination. We emphasize, however, that Rule 5104's "upon demand" language means that a firm should provide access at the time the staff requires access to be provided, and we do not expect the staff to suffer delays because of unsupported assertions that a privilege review cannot be completed quickly.

**Rule 5105 – Requests for Testimony or Production of Documents from Persons Not Associated with Registered Public Accounting Firms**

Section 105(b)(2)(C) of the Act authorizes the Board to promulgate rules to request that any person, including any client of a registered public accounting firm, provide any testimony and documents that the Board considers relevant or material to an investigation. The Act requires the Board and the staff to provide appropriate notice of such requests, subject to the needs of the investigation. Rule 5105 implements that authority by providing that the Board and the staff may make such requests to any

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person. In this context, the rules use the term "accounting board request" to distinguish it from an "accounting board demand," which may be made only to registered public accounting firms and associated persons of such firms.

Rule 5105 provides that the Board or staff shall give appropriate notice when requesting testimony (Rule 5105(a)(1)) and specify a reasonable time and place when requesting document production (Rule 5105(b)). What notice is appropriate for testimony, and what is a reasonable time and place for production, may vary with the circumstances and the needs of the investigation. Rule 5105(a)(1) also provides that an accounting board request for testimony shall state the method by which the testimony shall be recorded. The rule further provides that if the person to be examined is an organized entity, rather than a natural person, the accounting board request shall provide a description with reasonable particularity of the matters on which examination is requested.

Rule 5105(a)(2) incorporates, in the context of testimony pursuant to an accounting board request, the procedural and transcript provisions of testimony pursuant to an accounting board demand, as discussed above with respect to Rules 5102(c)-(e).

Although the Board can only request, and not require, testimony or production of documents from persons other than registered public accounting firms and associated

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persons of such firms, the Board does have the option of seeking a Commission subpoena to require testimony or document production from any person, as discussed below with respect to Rule 5111. The note to Rule 5105 serves as a reminder that this option is available to the Board. The note, however, does not in any way limit the Board's authority to seek a Commission subpoena at any time, even if the Board has not first sought the testimony or documents through an accounting board request. Neither the note, nor anything in the Board's rules, creates any right in any person to receive an accounting board request or any other form of notice from the Board before the Board seeks a Commission subpoena to be served on that person.

In response to comments, we have made technical changes to rule 5105(a)(2). Specifically, we have substituted the word "individual" for "person" where appropriate to avoid confusion that could flow from the fact that "person" is defined to include an entity.

#### **Rule 5106 – Assertion of Claim of Privilege**

Rule 5106 imposes requirements on any person who declines to provide testimony, documents, or information required by an accounting board demand, or a demand for examination under Rule 5104, on the ground of an assertion of privilege. The rule specifies the types of information that a person must supply related to the privilege assertion. The rule is adapted from Rule 6.2 of the local rules of the District

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Court for the Southern District of New York. Failure to supply the required information is a violation of the rule, and may subject a person to a disciplinary proceeding for violation of a Board rule or for noncooperation with an investigation.

Some commenters suggested that the rule should provide more flexibility so that a firm or associated person need not face the prospect of a noncooperation hearing and sanction for failure to supply all of the details that the rule requires in a privilege log. We have declined to modify the rule in this respect for two reasons. First, as a general matter, the information required will necessarily be readily available to the person asserting the privilege. Second, we note again our premise that the staff will act reasonably. We see no need to try to articulate by rule the line between noncooperation that warrants a disciplinary sanction and insignificant, technical shortcomings that do not.

One commenter suggested that the rule should provide that failure to comply with the privilege log requirements could not result in a noncooperation proceeding absent a showing that the required information was both readily available and necessary in order to assess the good faith of the privilege claim. We decline to follow this suggestion as well. The privilege log requirements are based on the reasonable premise that the information is by its nature readily available to the person asserting the privilege, and we see no reason to allocate to the staff the burden of establishing that fact. Nor do we

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see any sound basis for the suggestion that the staff should have to establish that the information is needed in order to assess the privilege claim.

Commenters also sought clarification on the nature and scope of privileges that may be asserted without being treated by the Board as noncooperation. We have not attempted to clarify the point in rule text. We note, however, that we do not intend to invade the province of any legitimately asserted privilege that would, under prevailing law, be treated as a valid basis for declining to provide documents or information in response to a Commission subpoena, including valid assertions of the privilege against self-incrimination under the Fifth Amendment to the United States Constitution. We fully intend, however, that assertions of the Fifth Amendment privilege may be used as evidence in Board disciplinary proceedings and will be the basis for evidentiary inferences against the person asserting the privilege. In addition, we may also report assertions of that privilege to other appropriate authorities consistent with our authority under the Act to share information.

One commenter specifically indicated a need for clarification on whether a state law accountant-client privilege may be asserted in response to Board requests for testimony, documents, or information. The Board will not honor assertions of an accountant-client privilege. Failure to comply with an accounting board demand on the basis of an asserted accountant-client privilege will be grounds for a noncooperation

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sanction. Likewise, any perceived state law nondisclosure requirements or other obstacles to compliance with an accounting board demand (other than a privilege that would be a valid basis for resisting a Commission subpoena) are, in our view, preempted by the Act, and a failure to comply on the basis of such requirements will be grounds for a noncooperation hearing and sanction.

Commenters also expressed concern that persons desiring in good faith to assert a privilege may have to choose between asserting the privilege or facing a noncooperation sanction if the staff and the Board view the assertion as not valid. That, however, is not necessarily the case.

As with disputes about the scope of an accounting board demand (discussed above), we expect that the staff, where appropriate, will recommend the institution of noncooperation proceedings when it cannot resolve privilege disputes. Again, however, this is not to say that a person proceeding reasonably and in good faith can only obtain Board review of the matter through a process that necessarily ends in a sanction if the Board sides with the staff. A noncooperation proceeding will normally include an opportunity for a person to submit a statement of position under Rule 5109(d). The Board will take that submission into account in determining whether to institute noncooperation proceedings.

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If the submission does not persuade the Board, a noncooperation proceeding will not necessarily follow. Some matters may involve good faith disputes about genuinely uncertain questions regarding the application of a privilege in the context of a Board investigation, or the application of a privilege to particular documents or communications. In those cases, the Board might communicate its rejection of the person's position but also indicate that noncooperation proceedings will not be commenced if the person complies with the demand within a certain time. At that point, the person could comply or, at the risk of a sanction, could continue to assert the privilege in the hope of prevailing before a hearing officer, or on review by the Board, the Commission, or the court of appeals.

As in the context of disputes about the scope of an accounting board demand, we should not be understood as suggesting that we will routinely afford an opportunity to cure noncompliance before authorizing noncooperation proceedings. We are not describing a process that effectively affords a mechanism for automatically delaying compliance with every accounting board demand. We will, based on the circumstances of each case, determine whether it is appropriate to afford an opportunity to cure before noncooperation proceedings are instituted, or whether a noncooperation proceeding is appropriate whether or not the noncompliance is cured. We may determine that the circumstances warrant a hearing on noncooperation and the possible imposition of a

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sanction even if the noncompliance is cured, while always holding out the possibility that curing the noncompliance may bear on the ultimate severity of any sanction.

**Rule 5107 – Uniform Definitions in Demands and Requests for Information**

Rule 5107 supplies certain definitions and rules of construction that shall be deemed to be incorporated by reference into all accounting board demands and accounting board requests for information. These definitions and rules of construction are modeled on those in use by the federal districts courts in the Southern District of New York. Rule 5107 does not preclude the Board or the staff, in any particular accounting board demand or accounting board request, from defining other terms, or from using abbreviations, or supplementing or using only part of a definition of a term defined in Rule 5107.

**Rule 5108 – Confidentiality of Investigatory Records**

Rule 5108 provides that unless otherwise ordered by the Board or the Commission, all documents, testimony, or other information prepared or received by or specifically for the Board or its staff in connection with an informal inquiry or a formal investigation shall be confidential in the hands of the Board, unless and until presented in connection with a public proceeding or released in accordance with Section 105(c) of the Act and the Board's rules thereunder. Consistent with Section 105(b)(5) of the Act, however, Rule 5108 provides that the Board may supply any such information to the

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Commission and, when determined by the Board to be necessary to accomplish the purposes of the Act or to protect investors, to certain other government entities, specifically: the Attorney General of the United States, an appropriate Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act) other than the Commission if the information pertains to an audit report for an institution subject to the jurisdiction of such regulator, state attorneys general in connection with any criminal investigation, and appropriate state regulatory authorities.

Commenters expressed several concerns and made several suggestions about proposed Rule 5108. We have made only one change to the rule in response to comments. Specifically, we have deleted the phrase "unless otherwise ordered by the Board or the Commission" from the beginning of the rule. Although the phrase was not intended to provide general discretionary authority to disclose confidential materials other than on the Act's own terms, we have instead adopted the rule with a new paragraph (b), which more precisely addresses the relevant point.

The new paragraph (b) provides that nothing in paragraph (a) "shall prohibit the Board or the staff of the Board from disclosing any documents, testimony, or other information to any other person as is reasonably necessary to carry out the Board's responsibility, under Section 105 of the Act, to conduct investigations according to fair procedures." The purpose of this provision is to provide notice that the Board does not

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interpret Section 105(b)(5)(A) to prohibit the Board from doing such fundamental things as, for example, questioning a witness about a document supplied to the staff by someone other than that witness.

Read literally and in isolation, Section 105(b)(5)(A) could be understood to prohibit the staff not only from showing exhibits to witnesses, but even from transmitting to a firm a written accounting board demand for documents, since the demand would be a document encompassed by the language of Section 105(b)(5)(A) and would therefore be confidential. We read Section 105(b)(5)(A) in light of, rather than in isolation from, the rest of Section 105. Section 105 begins by authorizing the Board to conduct investigations and requiring the Board to do so according to fair procedures. An overly literal reading of Section 105(b)(5)(A) would negate any possibility of doing so.

Rule 5108(b) reflects our understanding that the Act authorizes the Board and its staff to disclose documents and information (even if otherwise covered by Section 105(b)(5)(A)) as reasonably necessary to execute the Board's authority and responsibility to conduct fair investigations. Rule 5108(b)'s application does not extend outside the sphere of a Board investigation. It is not authority for disclosing information other than to a person from whom the Board demands or requests information in connection with an investigation. Even as to those persons, the rule is not authority for

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disclosing information other than as reasonably necessary to carry out legitimate investigative functions in a manner that is fair to the person.

Commenters also voiced other concerns about Rule 5108. For various reasons, however, we do not believe that any of these other concerns warrant changing the rule in the ways suggested by the commenters.

Commenters noted that the rule's confidentiality provision applies only to materials and information "in the hands of the Board," while Section 105(b)(5)(A) includes no such limiting phrase. Commenters suggested that the language of the Act contemplates that the protection of 105(b)(5)(A) extends much further, including to copies of documents that are prepared specifically for the Board, but that remain in the hands of the person who prepared them. One commenter suggested that the rule should expressly provide for confidentiality of documents in the hands of firms, associated persons, issuers whose audits are of concern in the investigation, and any witness who provides documents. The commenter also suggested that the rule should specify that the documents that are protected in the hands of such persons include originals and copies of transcripts, statements of position under Rule 5109(d), materials made available to a respondent under Rules 5422 and 5423, offers of settlement, and motions made during a disciplinary proceeding.

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We decline to make any changes along those suggested lines. The phrasing of the rule, however, is not intended to narrow the effect or the reach of the Act. Indeed, to try to avert any such misunderstanding, the first note to Rule 5108 describes what is provided in Section 105(b)(5) of the Act, as distinct from what is provided by Rule 5108. Our reason for limiting the wording of Rule 5108 has nothing to do with limiting the reach of Section 105(b)(5)(A), but, rather, has to do with limiting our rules to their appropriate reach. By using the phrase "in the Board's hands," we do not mean to express a view on whether the Act reaches further than that.

Similarly, the rule omits the Act's reference to an evidentiary privilege because, as to materials and information in the Board's hands, any evidentiary privilege the Board would assert would necessarily be based on the Act. The statute does not require an implementing rule in order for the Board to assert the privilege.

In contrast, we see value in implementing through Rule 5108 certain aspects of Section 105(b)(5), principally for purposes of notice concerning how the Board will comply with the requirements of 105(b)(5) (e.g., by keeping the relevant documents confidential) and that the Board will make appropriate use of its authority to share confidential materials with certain other regulators.

One commenter also suggested that the rules should reflect that the Board may enter into agreements with firms pursuant to which a firm could provide the Board with

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certain materials in which the firm may have a privilege, such as reports prepared by counsel concerning internal investigations, without waiving the privilege as to any third party.<sup>3/</sup> We decline to adopt this suggestion. We do not believe a rule is necessary in order to provide for the possibility of such protection in appropriate circumstances.

Commenters also suggested that the rule should do more to protect the confidentiality of documents that the Board provides to other agencies under Rule 5108(a)(1)-(2). Commenters suggested that the rule should make clear that the Act's provision requiring those agencies to maintain the materials as confidential and privileged preempts any state laws requiring open public access to records. Commenters also suggested that the rule should provide that the Board would only provide protected materials to an agency on the condition that the agency enter into a confidentiality agreement concerning the materials.

We do not doubt that Section 105(b) of the Act preempts state open records laws with respect to materials and information provided by the Board to an agency under

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<sup>3/</sup> The commenter noted that Commission staff has sometimes entered into such agreements, and that some courts have given effect to the agreements. See, e.g., Saito v. McKesson HBOC, Inc., 2002 WL 31657622 (Del. Ch. Nov. 13, 2002) and McKesson HBOC, Inc. v. Adler, 562 S.E.2d 809 (Ga. App. 2002).

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Section 105(b)(5)(B).<sup>4/</sup> Again, however, we do not see this as a point that has a place in the Board's rules. The Act speaks clearly for itself on this point.

For similar reasons, the rule does not seek to prohibit agencies from disclosing materials that the Act itself forbids them to disclose. Nor do we see a need to provide, by rule, for a confidentiality agreement in every case to reinforce the requirements of the Act. It is the Act, and not the Board's rules, that constrain the conduct of those agencies. In the event that we discover that any particular agency makes disclosures that we believe are inconsistent with Section 105(b)(5), both the Act and Rule 5108 allow us the flexibility to decline to supply certain information to that agency or to require appropriate assurances of confidentiality.

Finally, some commenters suggested that the rules should provide for some sort of notice to a firm or associated person when the Board provides documents or information to another agency. One commenter suggested that such notice be provided to the firm or person being investigated. The comment apparently means to suggest that such notice be provided to the firm or person being investigated, regardless of whether the documents being transmitted to an agency were supplied by the firm or

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<sup>4/</sup> Any otherwise applicable state or local law that would conflict with a requirement of the Act or stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress is preempted. See, e.g., Crosby v. National Foreign Trade Council, 530 U.S. 363, 372-73 (2000); City of New York v. FCC, 486 U.S. 57, 64 (1988).



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associated person being investigated. Other comments might also be understood to suggest that the notice be supplied to the firm or person who supplied the documents to the Board. Commenters suggested that such notice would be appropriate so that persons with an incentive to enforce the confidentiality provisions that restrict those agencies are in fact aware when the agencies obtain protected materials.

We have not included any notice requirement in the rule. We cannot identify any reasonable rationale for providing, as one commenter suggested, notice to a person who is not the person who supplied the Board with the documents that the Board is transmitting to an agency. The commenters' narrower suggestion that the rules should provide for notice to the person who actually supplied the documents or information to the Board raises a slightly different question, yet we still believe there are compelling reasons not to adopt such a notice requirement.

Most significantly, providing such notice might well undermine the legitimate investigative needs of the agency to whom the documents and information are supplied. With no clear indication in the Act that Congress intended or expected us to provide this type of notice, we are loathe to neglect the obvious interests of federal and state regulators and law enforcement agencies in maintaining the confidentiality of aspects of

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their processes.<sup>5/</sup> In addition, the notion that any fairness considerations require this type of notice has effectively been rejected by the Supreme Court in the context of Commission investigations. In S.E.C. v. Jerry T. O'Brien, Inc., 467 U.S. 735 (1984), the Court held, among other things, that general policy considerations did not entitle a person whose conduct was at issue in a Commission investigation to receive notice of Commission subpoenas directed to other persons in the investigation. One argument that the Court rejected – that the person was entitled to an opportunity to protect his rights with respect to Commission requests for information from others<sup>6/</sup> – is similar to an argument advanced by commenters here -- that notice would ensure them of an opportunity to enforce the confidentiality restrictions against the receiving agency.

The second note to Rule 5108 points out that the Director of Enforcement and Investigations may engage in, and may authorize staff to engage in, discussions with persons identified in Rule 5108 concerning documents, testimony, and information described in the rule.

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<sup>5/</sup> We also note that, in the context of Commission investigations, with very limited exceptions concerning certain of an individual's financial institution account records covered by the Right to Financial Privacy Act, 12 U.S.C. 3401, et seq., no notice is required or provided when the Commission shares documents or information with other regulatory or law enforcement agencies.

<sup>6/</sup> See 467 U.S. at 748-49.

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**Rule 5109 – Rights of Witnesses in Inquiries and Investigations**

Rule 5109 sets out certain rights accorded to persons from whom the Board seeks documents, testimony, or information in an investigation. Under Rule 5109(a), any person compelled to testify or produce documents pursuant to a Commission subpoena issued pursuant to Rule 5111, and any person who testifies or produces documents pursuant to an accounting board demand, shall, upon request, be allowed to review the Board's order of formal investigation. No such person is entitled to obtain their own copy of the order of formal investigation, but the Director of Enforcement and Investigations may, in his or her discretion, allow a person to obtain a copy of the order. This rule is adapted from Rule 7(a) of the Commission's Rules Relating to Investigations.

One commenter suggested that a copy of the formal order of investigation should be provided as a matter of right, subject to a person's agreement to certain restrictions on the use of the document. We have added to the rule a provision that the Director of Enforcement and Investigations may, as a condition of granting a request for the formal order, impose limitations on its further dissemination. We intend for the Director to use this discretion as necessary to avoid undermining an investigation and to maintain, to the extent reasonably possible, the nonpublic nature of the formal order. We do not intend that this discretion routinely be used in a way that would inhibit legitimate uses of

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the document by a person or counsel, such as sharing of the document subject to a joint defense agreement.

Under the rule we adopt, every person who receives an accounting board demand or an accounting board request has the right to review the formal order of investigation. We decline, however, to create for every such person a right to obtain a copy of the formal order. It is appropriate for the staff to exercise discretion not to provide the formal order, in light of legitimate investigative purposes and the general need to maintain the Board's investigative activity as confidential and nonpublic.

Rule 5109(b) allows any person who appears to testify in a formal investigation to be accompanied, represented, and advised by counsel. Rule 5109(b) grants this right on the condition that counsel affirmatively represents to the staff, either through a notice of appearance or a statement on the record at the beginning of the testimony, that he or she represents the witness. This rule is adapted from Rule 7(b) of the Commission's Rules Relating to Investigations. The right granted by Rule 5109(b) is also limited by Rule 5102(c)(3), which does not allow for the presence of any person, even counsel, who has been or is reasonably likely to be examined in the investigation.

Rule 5109(c) provides that a witness may inspect the transcript of his or her own testimony. A person who has testified or provided documents may also request a copy of his or her transcript or of the documents he or she produced. If the request is

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granted, the transcript or documents may be obtained upon the payment of fees to cover the cost of reproduction. Any such request, however, may be denied by the Director of Enforcement and Investigations for good cause shown if the documents or testimony have not been presented in connection with a proceeding or released in accordance with Section 105(c) of the Act and the Board's rules thereunder. This rule is adapted in part from Rule 6 of the Commission's Rules Relating to Investigations.

One commenter suggested that the rule should provide a mechanism for the Director to make the determination whether "good cause" exists for denying copies to a witness, and that the rule should provide for review of the Director's decision. We decline to adopt these suggestions. The purpose of this aspect of the rule is to commit the matter to the Director's discretion. A person may always inspect the transcript of his or her own testimony, but the Director will have the discretion to preclude any witness from having his or her own copy of the transcript.

Rule 5109(d) provides that registered public accounting firms and persons associated with such firms may, on their own initiative at any time, submit a written statement to the Board setting forth their interests and positions in regard to the subject matter of any investigation in which they have become involved. The staff, either upon request or on its own initiative, may – but is not required to – advise any such person of the general nature of an investigation, including the indicated violations as they pertain



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to that person, and may prescribe a fixed period of time that will be allowed for the person to submit a statement of position and interests before the staff makes any recommendation to the Board. Rule 5109(d) provides that any such statement that is submitted will be forwarded to the Board in conjunction with any staff recommendation pertaining to the person submitting the statement. This rule is adapted from Rule 7(a) of the Commission's Rules Relating to Investigations.

Commenters made several suggestions about the proposed Rule 5109(d) process. They suggested that the rule should require that this opportunity be afforded to a prospective respondent as a matter of right, that reasonable and sufficient time always be allowed for the preparation of a submission, and that the prospective respondent should have access to the investigative record in order to prepare a more meaningful submission. We have declined to change the rule in response to these suggestions.

The purpose of the Rule 5109(d) process is to assist the Board in its decision-making. It is not to protect or to create any supposed right to be heard at this stage of a matter. It is our expectation that the staff will routinely give a respondent a meaningful opportunity to make a Rule 5109(d) submission. We also expect, though, that the staff will exercise its discretion not to provide that opportunity when doing so would be contrary to the public interest or the interests of investors – such as when



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circumstances call for expedited enforcement action, or when advance notice of particular charges to a respondent might undermine legitimate investigative objectives of the Board or of other regulatory or law enforcement agencies conducting parallel investigations. We therefore decline to create a right to make a Rule 5109(d) submission, or a right to have a certain amount of time in every case where the opportunity is afforded.

We also decline to require that a prospective respondent have access to any portion of the investigative record in connection with making a Rule 5109(d) submission. The Rule 5109(d) process, which is based on the Commission's so-called "Wells" process, provides a meaningful opportunity for a prospective respondent to focus the Board's attention on significant issues concerning the prospective respondent's characterization of its own conduct, and on legal and policy issues implicated by the staff's recommendation. The process usefully serves these purposes without becoming a miniature adjudication in which the prospective respondent provides its characterization of all of the evidence in the investigative record.

#### **Rule 5110 – Noncooperation with an Investigation**

Section 105(b)(3) of the Act authorizes the Board to impose sanctions, including revocation of registration and bar on association, against any registered public accounting firm or associated person who refuses to testify, produce documents, or

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otherwise cooperate with the Board in connection with an investigation. Rule 5110 describes how the Board will implement that authority.

Under Rule 5110(a), the Board may institute a disciplinary proceeding, in accordance with Rule 5200(a)(3), for noncooperation with an investigation in certain circumstances. Under the rule as proposed, a noncooperation proceeding would have been warranted if it appeared to the Board that a registered public accounting firm or an associated person may have failed to comply with an accounting board demand, may have given testimony that is false or misleading or that omits material information, or may otherwise have failed to cooperate in connection with an investigation.

Commenters raised various concerns with this aspect of the proposal. First, commenters echoed other comments, discussed above, concerning a need to have some mechanism for review of staff positions (on such things as privilege disputes and the scope of document demands) without having to risk a noncooperation proceeding for noncompliance. We have effectively addressed the substance of those comments in our discussions of Rule 5103(a) and 5106.

Commenters also expressed concern about the prospect of a noncooperation proceeding for providing testimony that "omits material information." After consideration of the comments, we agree that the scope of the proposed rule should be revised on this point. We have therefore deleted the language concerning testimony that is false or

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misleading or that omits material information. In its place, we have substituted the language of the federal perjury statute, 18 U.S.C. § 1623. The final rule provides for instituting a noncooperation proceeding where it appears to the Board that a person may have "knowingly made any false material declaration or made or used any other information, including any book, paper, document, record, recording, or other material, knowing the same to contain any false material declaration."

One commenter also requested clarification on what would be considered noncooperation. We decline to attempt to set out every way in which a firm or associated person may fall short of its statutory obligation to cooperate with the Board in connection with an investigation. We believe it is appropriate to continue to include in the rule the general provision, echoing the Act, that noncooperation proceedings may be instituted where a firm or associated person "may otherwise have failed to cooperate." Depending upon the nature of the conduct, however, it may be appropriate in many circumstances for the staff to provide notice that it views certain conduct as noncooperation, and to afford an opportunity to cease or cure the conduct before recommending noncooperation proceedings.

In response to the request for clarification, we have added one additional point to the list of items that may warrant institution of noncooperation proceedings. Specifically, the rule we adopt states that we may authorize noncooperation

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proceedings where it appears that a firm or associated person may have abused the Board's processes for the purpose of obstructing an investigation.

This new provision grew out of a comment made in connection with Rule 5402. The commenter suggested that the Board should impose fines for frivolous interlocutory appeals. We agree that abuse of the Board's processes is a form of failing to "otherwise cooperate," and we have added this provision to Rule 5110 to provide notice that the Board will impose sanctions for this form of noncooperation. In the interest of fairness, we have drafted the provision to include a scienter requirement: we will not treat as noncooperation every arguable abuse of the Board's processes, but only those that involve an intent to obstruct an investigation. We may, however, infer such an intent from circumstantial evidence, including, for example, circumstances indicating that a reasonable person would not have believed there was any genuine chance of prevailing on a particular petition for review of staff action or of a hearing officer ruling short of finding a violation.<sup>7/</sup>

A disciplinary proceeding for noncooperation shall proceed generally according to the hearing procedures set out in the Board's rules. Because of the nature of the conduct being sanctioned, however, a disciplinary proceeding for noncooperation will generally be a streamlined proceeding focused on a narrow issue. For that reason,

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<sup>7/</sup> In no circumstance will a party's petition for review of a hearing officer's initial decision finding a violation by that party be treated as noncooperation.

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various of the procedural rules governing disciplinary proceedings include certain provisions that will apply only to disciplinary proceedings for noncooperation.

Some commenters expressed doubts about the appropriateness of a streamlined procedure for noncooperation proceedings. These commenters stated that noncooperation proceedings will present very complex factual and legal issues, and that the rules should not be based on a presupposition that these will be simple matters.

We recognize that some noncooperation proceedings may present complex legal issues. Some, such as those involving allegations of false testimony, may also involve significant factual evidence. The rules that we have proposed and adopted provide sufficient flexibility to deal with complex noncooperation issues in an appropriate time frame. But the rules are also designed to address, during the course of an investigation, ongoing recalcitrance even in the absence of any significant factual or legal issue. The rules afford a streamlined approach that will allow for swift dealing with that type of recalcitrance, but the streamlined option should not be understood as a signal that the Board intends to give short shrift to genuinely complex factual and legal issues that may arise in the noncooperation context.

One commenter requested clarification as to whether a firm might be held responsible for the noncooperation of one of its associated persons. Nothing in the rules creates vicarious noncooperation liability for a firm. Nevertheless, an associated

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person's noncooperation has consequences for the firm. Pursuant to section 102(b)(3) of the Act and the Board's rules, every registered public accounting firm will have agreed, as a condition of the continuing effectiveness of its registration, (1) to secure from each of its associated persons a consent to cooperate in and comply with Board demands, and (2) to enforce those consents. While the firm would face no vicarious liability for the associated person's noncooperation, the firm's own registration status would be at risk if the firm failed either to secure the associated person's cooperation with the Board or to end its association with the person.

**Rule 5111 – Requests for Issuance of Commission Subpoenas in Aid of an Investigation**

Section 105(b)(2)(D) of the Act authorizes the Board to promulgate rules according to which the Board may seek issuance by the Commission, in a manner established by the Commission, of a subpoena on any person to require testimony and the production of documents that the Board considers relevant or material to an investigation. Rule 5111 implements that authority by providing that the Board shall seek issuance of such subpoenas, and in seeking such subpoenas shall supply the Commission with a completed form of subpoena and such other information as the Commission may require.

One commenter suggested that the rule should provide that any judicial action to enforce a Commission subpoena arising out of a Board investigation will be filed under

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seal, to maintain the confidentiality of the matter. We decline to adopt this suggestion because it appears to be more about Commission processes than about Board processes.

**Rule 5112 – Coordination and Referral of Investigations**

Rule 5112(a) provides that the Board will notify the Commission of any pending investigation that involves a potential violation of the securities laws. The rule provides that the Board will do so as soon as practicable after entry of an order of formal investigation by sending a copy of the order to the Commission or appropriate Commission staff. Rule 5112(a) provides that the staff will then coordinate its work with the Commission's Division of Enforcement as necessary to protect any ongoing Commission investigation.

Rule 5112(b) provides that the Board may refer any investigation to the Commission and, in the case of an investigation that concerns an audit report for an institution that is subject to the jurisdiction of any other Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act), to that regulator.

Rule 5112(c) provides that, at the direction of the Commission, the Board may refer any investigation to the Attorney General of the United States, the attorney general of one or more states, and an appropriate state regulatory authority.



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One commenter asked that the rule make clear that Board cooperation with other agencies does not extend to initiating investigations in aid of another agency's parallel proceedings. We decline to make this point in the rule. In this context, concepts like "in aid of" are too nebulous to be meaningful and serve only to fuel resource-consuming peripheral disputes. The Board will exercise all of its authority in a manner that it believes to be consistent with the Act. Disputes concerning whether the Board's reasons for initiating any particular investigation are appropriate may be addressed by reference to the Act.

Another commenter suggested that the rules should implement section 105(d)(1)(B) of the Act, which requires that the Board report any disciplinary sanction to the appropriate state regulatory authority or any foreign accountancy licensing board with which the disciplined firm or associated person is licensed or certified. In addition to state and foreign authorities, section 105(d)(1) also requires the Board to report sanctions to the Commission (section 105(d)(1)(A)) and, at the appropriate time, the public (section 105(d)(1)(C)). These provisions govern the Board, without providing for any discretion, and do not require an implementing rule.



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## **Part 2 – Disciplinary Proceedings**

Part 2 of the Board's Rules on Investigations and Adjudications consists of Rules 5200 through 5206. These rules address the commencement of disciplinary proceedings and the elements of those proceedings.

### **Rule 5200 – Commencement of Disciplinary Proceedings**

Rule 5200 addresses the commencement of disciplinary proceedings and certain related matters. Rule 5200(a) identifies the three general categories of circumstances under which the Board may commence a disciplinary proceeding: when it appears to the Board that a hearing is warranted to determine whether (1) a registered public accounting firm or a person associated with such a firm has engaged in any act or practice, or omitted to act, in violation 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 issued under the Act, or professional standards, (2) such a firm, or its supervisory personnel, has failed reasonably to supervise an associated person, either as required by the Rules of the Board relating to auditing or quality control standards, or otherwise, with a view to preventing violations of laws, rules, and standards, or (3) such a firm or a person associated with such a firm has failed to comply with an accounting

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board demand, given false testimony, or otherwise failed to cooperate in connection with an investigation.

One commenter questioned whether "appears to the Board" is a sufficiently high standard and suggested that the rule require the Board to find a "reasonable basis" for concluding that a violation has occurred. We believe that "appears to the Board" is the appropriate standard. In the context of authorizing a disciplinary proceeding, the Board members' views on whether there is sufficient reason to believe that a violation occurred and is likely to be proven are sufficient. The use of an objective standard would have no practical effect on the outcome of the Board's deliberations and, if anything, would serve only as a peripheral litigation issue when the parties should instead be focused on the question of liability, rather than the question of whether the Board had sufficient reason to authorize the action.

Another commenter requested clarification on whether a violation based on a single negligent act is sufficient grounds to institute a disciplinary proceeding. The Act plainly contemplates that disciplinary proceedings can be instituted for a violation based on a single negligent act. Section 105(c)(5) of the Act provides that the Board may impose the more severe sanctions authorized by section 105(c)(4) only in cases that involve intentional or knowing conduct (including reckless conduct) or repeated instances of negligent conduct. Implicit in that provision is that a violation based on a

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single instance of negligent conduct is sufficient to warrant a disciplinary proceeding to impose lesser sanctions.

Commenters also suggested that the Board should provide guidance concerning the term "supervisory personnel," and the concept of liability for a "failure to supervise." One commenter suggested that the Board should limit "supervisory personnel" to the partner in charge of an audit and an audit manager, and that the Board should spell out what constitutes a failure of reasonable supervision. Commenters made the point that supervisory structures of accounting firms are very different from supervisory structures at broker-dealers, and that therefore Commission precedent on failure to supervise can provide no guidance.

At this time, we are not providing specific guidance on the scope of supervisory liability under the Act. We will continue to consider whether additional guidance or rulemaking on this point would be appropriate. We see no reason, however, to limit the persons who may have supervisory liability to those occupying certain positions. A firm itself may have liability for failure to supervise, as may any associated person who plays a supervisory role. Moreover, even in the absence of additional, specific guidance, investigations may uncover circumstances in which it would be appropriate, under any reasonable reading of the Act, to commence disciplinary proceedings for failure to supervise.

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Rule 5200(b) provides for an appointment of a hearing officer by the Board as soon as practicable after issuance of the order instituting proceedings or after a registration applicant has requested a hearing pursuant to Rule 5500(b). The rule is adapted from NASD Rule 9213(a). Under Rule 5200(b), the Board shall notify the parties of the hearing officer's assignment. The hearing officer shall have authority to do all things necessary and appropriate to discharge his or her duties, including, but not limited to, the matters specified in Rule 5200(b). The rule expressly subjects the hearing officer's authority to the limitations described in Rule 5402 (concerning hearing officer disqualification) and Rule 5403 (concerning *ex parte* communications). Though not part of the proposed rule, we have added the provision concerning registration hearings to conform this rule to the substance of the other provisions concerning hearings on disapproval of registration applications.

One commenter suggested that the rule should expressly provide the hearing officer with power to resolve disputes concerning document disclosure and the power to perform all other duties authorized elsewhere in the rules. We believe that the rule, as proposed and adopted, gives such authority to the hearing officer by virtue of the authority to rule on motions and to do all things necessary and appropriate to discharge duties.

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Rule 5200(c) provides that the Board will observe certain separation of functions principles. The proposed rule provided that any Board employee or agent engaged in investigative or prosecutorial functions for the Board in a proceeding could not, in that same proceeding or a factually related proceeding, participate or advise in the decision, or in Board review of the decision, except as a witness or counsel in the proceeding.

One commenter suggested that this rule should clearly exclude all enforcement personnel from participating in the adjudication of a disciplinary proceeding, whether or not they had an investigative or prosecutorial role in the matter. We are persuaded that this represents a good policy choice and we have revised the rule accordingly. The final rule provides that neither the staff of the Division of Enforcement and Investigations, nor any other staff who engaged in investigative or prosecutorial functions on a matter, may participate or advise in the decision, or the review of the decision, except as a witness or counsel. In addition, the rule provides, as proposed, that a hearing officer may not be responsible to or subject to the supervision or direction of an employee or agent engaged in the performance of investigative or prosecuting functions for the Board.

With respect to proceedings that involve a common question of law or fact, Rule 5200(d) provides that the Board or a hearing officer may, by order, consolidate the proceedings for hearing of any or all matters at issue in the proceedings. The rule is adapted from Rule 201 of the Commission's Rules of Practice. The rule provides that

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consolidation shall not prejudice any rights that any party may have under the Board's Rules and shall not affect the right of any party to raise issues that could have been raised in the absence of consolidation.

Commenters suggested that the Board should recognize that consolidation may prejudice one or more parties and should allow parties an opportunity to object to joinder. One commenter stated that the rules should incorporate the standard for joinder under the federal rules, which the commenter characterized as allowing consolidation only when claims arise out of the same transaction or occurrence.

We have not changed the rule in response to the comments. The rule reflects an awareness of the possibility that consolidation could prejudice one or more parties. The rule specifically provides that matters may not be consolidated if doing so would prejudice a party's rights, and the rules afford the hearing officer an opportunity to hear any objections to consolidation. Where consolidation does not prejudice a party, then consolidation should not be objectionable, and may on occasion be appropriate and efficient, even when the commonality is limited to a question of law.

#### **Rule 5201 – Notification of Commencement of Disciplinary Proceedings**

Rule 5201(a) provides that when the Board issues an order instituting proceedings, the Secretary shall give each person or firm charged appropriate notice of the order within a time reasonable in light of the circumstances. As described in the

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note to Rule 5201(a), in the case of emergency or expedited action, actual notice – by any means reasonably calculated to supply notice – may precede formal service of the order instituting proceedings.

One commenter suggested that the rule should be more specific on the timing of notice, or should at least provide that in no event would notice be provided later than 30 days after the issuance of the order. We have not adopted this suggestion. It is in the Board's interest to effect notice of the order as soon as possible after issuance. There is no strategic or other advantage to the Board in delaying notice, and the existence of the unserved order works no prejudice to, and imposes no obligations on, the respondent.

Another commenter suggested that the rule should specify the amount of notice that a respondent would have before a hearing would begin. This commenter suggested that the rule provide that a hearing could not begin sooner than 60 days or 90 days after notice of the order instituting the proceeding. A second commenter suggested that no hearing should commence sooner than 90 days after notice of the order instituting the proceeding.

We agree that the rule should include a provision concerning notice of the hearing date, though we decline to specify the suggested time frames. Rather, we have added a provision to rule 5201(a) providing that if the order instituting proceedings sets

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a hearing date, each party shall be given notice of the hearing within a time reasonable, in light of the circumstances, in advance of the hearing. As a general matter, we expect that Board orders instituting proceedings will not specify a hearing date, unless the proceedings are for noncooperation. In those proceedings, we may find that reasonable notice of a hearing date is less than 90 days or 60 days, and we decline to provide by rule for a longer minimum time that would delay the process even when there is no genuine need for delay.

In matters where the Board's order does not set a hearing date, the hearing officer retains discretion to schedule a hearing date. We expect hearing officers to exercise that discretion prudently and fairly, consistent with avoiding unnecessary delays, but we decline to specify a minimum amount of notice that a party must have before a hearing may be held.

Rule 5201(b) describes the content of an order instituting proceedings. The precise requirements concerning the content of the order vary depending upon whether the proceeding is commenced under Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5200(a)(3). The proposed rule provided that, in each case, the order would specify in reasonable detail, with respect to each firm or person charged, the conduct alleged to form the basis for a disciplinary sanction.

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Commenters suggested that the rule should require more in the way of notice.

One commenter said that "reasonable detail" was insufficient, and that the rule should require a description of the time period, the alleged misconduct, and the alleged mental state with which the respondent acted. Another commenter suggested that the Board consider a heightened pleading requirement like that of Rule 9(b) of the Federal Rules of Civil Procedure.

We have modified the proposal to eliminate the phrase "reasonable detail." Instead, the rule requires a "short and plain statement of the matters of fact and law to be considered and determined," including of the conduct alleged to constitute a violation and the rule, statutory provision, or standard violated. Where a violation requires a particular state of mind, then a necessary component of alleging the conduct is alleging the existence of that state of mind. In requiring that the order include a description of the "conduct," the rule necessarily requires more than just a conclusory statement that the respondent engaged in conduct that violated a rule, statute, or standard. The rule requires that the order allege the conduct in sufficient factual detail to advise the respondent of what conduct is at issue.

Rule 5201(c) provides that, in the case of a hearing on a registration application commenced under Rule 5500, the notice of hearing shall state proposed grounds for disapproving the registration application.

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Rule 5201(d) provides that either the Board or, on the motion of the interested division, a hearing officer, may amend an order instituting proceedings. The Board may do so at any time to include new matters of fact or law. A hearing officer may do so only prior to the filing of an initial decision or, if no initial decision is to be filed, prior to the time fixed for filing final briefs with the Board. A hearing officer may amend an order only to include new matters of fact or law that are within the scope of the original order instituting proceedings, but may not initiate new charges or expand the scope of matters set for hearing beyond the framework of the Board's order instituting proceedings. The rule is adapted from Rule 200(d) of the Commission's Rules of Practice.

Commenters suggested that the ability to amend an order should be limited to adding questions of law or fact germane to those already included, that the Board should provide notice that it is considering amending an order, and that the Board should not amend an order when doing so would unfairly prejudice a respondent. We decline to change the rule in response to these comments. Concerns about notice and prejudice are less appropriately directed to whether amendment is allowed, and more appropriately addressed to whether a respondent is given a fair opportunity to address new matters after amendment of an order. We expect that hearing officers will exercise appropriate discretion in assuring a fair opportunity to address new matters added by amendment. As to the commenters' concerns about the scope of the allowable



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amendment, the rule already limits the hearing officer's amending authority to matters within the scope of the original order instituting proceedings. We decline to impose the same limitation on the Board's own authority to amend an order, though we reiterate that a respondent is entitled to a fair opportunity to address new matters added by amendment.

### **Rule 5202 – Record of Disciplinary Proceedings**

Rule 5202(a) describes the material that shall make up the contents of the record in a disciplinary proceeding (Rule 5202(a)(1)) and the contents of the record on disapproval of an application for registration (Rule 5202(a)(2)). Under Rule 5202(b), any document offered as evidence but excluded, and any document marked for identification but not offered as an exhibit, shall not be considered part of the record but shall be maintained by the Secretary until all opportunities for Commission and judicial review have been exhausted or waived. Paragraphs (c)-(e) of Rule 5202 address the substitution of true copies for documents in the record, the preparation of the record and the certification of the record index, and the final transmittal of record items to the Secretary. The rule is adapted from Rules 350 and 351 of the Commission's Rules of Practice.



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### **Rule 5203 – Public and Private Hearings**

Section 105(c)(2) of the Act provides that any proceeding by the Board to determine whether to discipline a registered public accounting firm or an associated person thereof shall not be public unless otherwise ordered by the Board for good cause shown, with the consent of the parties to the hearing. Rule 5203 implements that requirement by providing that proceedings commenced pursuant to Rule 5200(a) shall not be public unless the Board so orders, for good cause shown, with the consent of the parties.

Rule 5203 also provides that all other Board hearings shall be nonpublic unless the Board otherwise orders. In practical effect, this provision applies only to a hearing on disapproval of a registration application, since that is the only type of hearing for which the rules provide other than the hearings expressly covered by Section 105(c)(2) of the Act. The rule essentially creates a presumption that a hearing on disapproval of a registration application will be non-public. A disapproval hearing will, by its nature, involve a firm that is not yet a registered firm and may well involve a record that includes confidential information submitted as part of the registration application. The rule reserves to the Board the flexibility to make the hearing public if warranted by unusual circumstances. In any event, if the Board decides, after a hearing, to disapprove the



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application, that decision, along with the reasons for the decision, will be made public according to the provisions of Section 105(d) of the Act.

One commenter asked for clarification on whether the absence of one party's consent to a public proceeding would be sufficient to keep the proceeding nonpublic. Other than in hearings on disapproval of a registration application, it is correct that any one party's refusal to consent to a public proceeding is sufficient to keep the proceeding nonpublic. A hearing on disapproval of a registration application shall be nonpublic unless the Board, in its discretion, orders otherwise.

#### **Rule 5204 – Determinations in Disciplinary Proceedings**

One commenter expressed a concern that the proposed rules do not provide for the burdens of proof in a disciplinary proceeding. In response, we have added a new Rule 5204(a). Rule 5204(a) provides that in any disciplinary proceeding instituted pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5200(a)(3), the interested division shall bear the burden of proving an alleged violation or failure to supervise by a preponderance of the evidence.

We have adopted the rest of Rule 5204 as proposed, except for renumbering the paragraphs in light of the addition of a new paragraph (a). Rule 5204(b) provides that, unless the Board orders otherwise, the hearing officer shall prepare an initial decision following a hearing. The rule provides that the initial decision shall include findings and

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conclusions, including sanctions, if appropriate, and the reasons or basis therefore, as to all the material issues of fact, law, or discretion presented on the record and such other information as the Board may require. The rule is adapted from Rule 360 of the Commission's Rules of Practice.

The note to Rule 5204(b) sets out the Board's general expectations about the time frame within which a hearing officer should complete an initial decision in various types of cases. These time frames are nothing more than the Board's general expectations and do not create any right in any person to have an initial decision prepared within any particular period of time.

Rule 5204(c) governs the hearing officer's filing of the initial decision with the Secretary and the Secretary's service of the initial decision on the parties.

Rule 5204(d) provides the circumstances in which an initial decision of a hearing officer becomes the final decision of the Board as to a party. The rule is adapted from Rule 360(d) of the Commission's Rules of Practice. Rule 5204(d)(1) provides that the initial decision becomes the Board's final decision as to a party upon issuance by the Secretary of a notice of finality. Rule 5204(d)(2) provides that the Secretary shall issue the notice of finality no later than twenty days after the lapsing of the time period for filing a petition for Board review (as described in Rule 5460), unless one of the two conditions described in Rule 5204(d)(3) has occurred. Rule 5204(d)(3) provides that

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the Secretary shall not issue a notice of finality as to any party who has filed a timely petition for Board review or with respect to whom the Board, on its own motion, has ordered review of the initial decision pursuant to Rule 5460(b).

**Rule 5205 – Settlement of Disciplinary Proceedings Without a Determination After Hearing**

Rule 5205 governs certain matters related to possible settlement of disciplinary proceedings. The rule is adapted from Rule 240 of the Commission's Rules of Practice.

Rule 5205 provides that any person who is or is to be a party to a disciplinary proceeding may at any time propose in writing an offer of settlement. The rule imposes requirements for the content of the offer, and requires that it be signed by the person making the offer, not by counsel.

Rule 5205(c)(1) requires that the Director of Enforcement and Investigations present the offer to the Board along with a recommendation concerning the offer, except that, if the recommendation is unfavorable, the Director shall not present the offer to the Board unless the person making the offer so requests.

Rule 5205(c)(2)-(3) set out various matters that the person making the offer must waive before the Board will consider the offer, including waiver of rights to hearings, rights to proposed findings of fact and conclusions of law, rights to proceedings before and an initial decision by a hearing officer, rights to post-hearing procedures, rights to judicial review, rights to have Board and Board staff observe separation of functions

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principles, and rights to claim bias or prejudgment by the Board based on consideration of or discussions concerning the settlement offer.

Rule 5205(c)(4) provides that if the Board rejects the offer, the offer will be deemed withdrawn and will not constitute a part of the record. Rule 5205(c)(4) further provides that rejection of the offer will not affect the continued validity of waivers of rights to claim bias or prejudgment on the basis of discussions concerning the settlement offer.

Rule 5205(c)(5) provides that Board acceptance of an offer will occur only upon the issuance of findings and an order by the Board.

A note to Rule 5205 points out that in hearings on disapproval of registration, settlement offers will be handled by the Director of Registration and Inspections, rather than the Director of Enforcement and Investigations, in accordance with Rule 5205.

One commenter suggested that the rule should allow for conditional settlements that do not require waiver of appeal rights – in other words, settlements that are conditional, depending upon the resolution of a legal point on appeal. We decline to revise the rule to provide for this specifically, because we believe that, to the extent such a settlement might ever be appropriate, the rule as drafted accommodates it. In effect, the Board retains the flexibility to waive, in settlement, any of the waiver requirements that Rule 5205 imposes on respondents.

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One commenter suggested deleting Rule 5205(c)(3)(i), because it allows the staff to advise the Board concerning a settlement offer without the respondent being able to address what the staff says. We do not adopt this suggestion.

Settlement offers may frequently arise even before the Board has authorized a disciplinary proceeding. In that circumstance, discussions between the staff and the Board are "deliberations of the Board and its employees . . . in connection with . . . an investigation" and are privileged and confidential under section 105(b)(5)(A) of the Act.

Even if a settlement offer arises after the institution of a disciplinary proceeding, established regulatory practice, even among federal agencies subject to the procedural constraints of the Administrative Procedure Act, recognizes that a regulatory body functioning both as ultimate adjudicator and as a party is entitled to the confidential recommendations of its staff on settlement discussions, so long as the respondent waives prejudgment issues. The rule we adopt is consistent with that established practice. A respondent who wishes for us to consider a settlement offer must allow us to confer confidentially with the staff about the matter, and that requires that the respondent waive any right to assert prejudgment arguments based on those communications.

Commenters also suggested that the rule should provide that settlement negotiations and offers are privileged and confidential and, if no settlement is reached,

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may not be used as evidence in the proceeding itself. We fully expect that the content of settlement negotiations would not be introduced as evidence in Board proceedings, but we expect for that and any understandings about confidentiality to be accomplished in the same way it is in other contexts, such as Commission proceedings – by letter agreements and other agreements specific to the matter and the negotiation.

It is not clear, however, what the commenter means by suggesting that a Board rule should provide that settlement negotiations are "privileged." The Board intends to maintain the confidentiality of such negotiations, but whether such negotiations are privileged is not a matter for a Board rule.

### **Rule 5206 – Automatic Stay of Final Disciplinary Actions**

Rule 5206 provides that no final disciplinary sanction of the Board shall be effective until either (a) the dissolution by the Commission of the stay provided by Section 105(e) of the Act or (b) the expiration of the period during which the Commission, on its own motion or upon application under Section 19(d)(2) of the Exchange Act, may institute review of the sanction.

### **Part 3 – Disciplinary Sanctions**

Part 3 of the Board's Rules on Investigations and Adjudications consists of Rules 5300 through 5304. These rules describe the sanctions the Board may impose in



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disciplinary proceedings and various matters related to the effect of, and the termination of, such sanctions.

### **Rule 5300 – Sanctions**

Rule 5300 describes sanctions that the Board may impose in disciplinary proceedings. Rule 5300(a) describes sanctions that the Board may impose in disciplinary proceedings instituted other than for noncooperation in an investigation. Subparagraphs (1) – (6) of Rule 5300(a) incorporate the sanctions expressly provided by Section 105(c)(4) of the Act, including revocation of registration, bar from association, suspensions, limitations on activities, civil money penalties, censures, and a requirement of additional professional education or training. A Note to subparagraph (3) of Rule 5300(a) contains a non-exclusive list of types of limitations on activities the Board may impose. Subparagraphs (7) – (10) of Rule 5300(a) identify other sanctions, pursuant to the authority given to the Board in Section 105(c)(4)(G) of the Act, including requiring a party to engage an independent monitor, to engage counsel or other consultants to design policies to effectuate compliance with the Act, to adopt or implement policies or undertake action to improve audit quality or to effectuate compliance with the Act, or to obtain an independent review and report on one or more engagements.



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Commenters suggested that the rules should provide guidance on when particular sanctions will be imposed. Commenters sought assurance that revocation and bar would be reserved for the most serious matters. Commenters sought some articulation of the standard that must be met for the imposition of lesser sanctions.

We have not revised the rule in response to these comments. The more serious the violation is, the more severe the appropriate penalty will be, and the Board retains discretion to assess the seriousness of the violation and the severity of the penalty. In addition, section 105(c)(5) of the Act requires scienter or repeated negligence for imposition of the most severe sanctions. The Act does not limit the standard that must be met for imposition of other sanctions.

Rule 5300(b) describes the sanctions that the Board may impose in disciplinary proceedings for noncooperation with an investigation. The sanctions include revocations, bars, and suspensions, as expressly provided by Section 105(b)(3)(A) of the Act. Rule 5300(b) also identifies other sanctions, pursuant to the authority given to the Board in Section 105(b)(3)(A)(iii), including civil money penalties, censures, limitations on activities, requiring a firm to engage a special master or independent monitor to monitor and report on the firm's compliance with accounting board demands, or authorizing the hearing officer to retain jurisdiction to monitor compliance with accounting board demands.

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One commenter noted that the rules were unclear on whether money penalties might be assessed for noncooperation. The rule, as proposed and adopted, does provide for the possible imposition of money penalties for noncooperation.

Another commenter expressed doubt that the Act authorizes the imposition of money penalties for noncooperation. Section 105(b)(5) of the Act provides that noncooperation may be punished by revocation, bar, suspension, and "such other lesser sanctions as the Board considers appropriate." We believe that an appropriately calibrated money penalty is a "lesser sanction" than revocation of a firm's registration or a bar on association with a firm.

The commenter argued that "lesser sanctions" should be understood to mean only those sanctions, such as censure or additional training, for which section 105(c)(5) of the Act does not prescribe a scienter requirement. We see two significant flaws in this reasoning. First, the reasoning is premised on the notion that noncooperation, by its nature, does not involve scienter. This is not correct for all forms of noncooperation. Some instances of noncompliance will be evident on their face – for example, a failure to provide documents required by an accounting board demand – and are sanctionable as noncooperation without the need to establish any scienter. Other instances of noncooperation, such as knowingly providing false testimony or abusing Board processes to obstruct an investigation, necessarily involve a scienter element, and

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would be punishable by a money penalty even if the Act limited money penalties to scienter-based offenses.

Second, the Act, in fact, does not limit money penalties to scienter-based offenses. Section 105(c)(5) distinguishes between money penalties that do require a finding of scienter (money penalties greater than \$100,000 for a natural person or \$2,000,000 for any other person) and money penalties that do not require a finding of scienter (all other money penalties). Accordingly, even under the commenter's own rationale – that "lesser sanctions" means only those sanctions available for non-scienter offenses – money penalties would be among those sanctions.

When the Board revokes a firm's registration or bars a person from association with a registered public accounting firm, the sanction is permanent and will not expire of its own accord. In contrast, a suspension of registration or a suspension from association shall be for a fixed time period at the expiration of which a suspended firm shall resume its status as registered and a suspended person shall be free to associate with a registered firm.

In the case of a revocation of registration or a bar on association, the Board may provide for a specified period after which the firm may reapply for registration, or the person may petition for termination of the bar. Modification or termination of sanctions is discussed below in connection with Rule 5302.

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A note to Rule 5300 points out that the rule does not preclude the imposition, on consent in the context of a settlement, of any other sanction not identified in the rule.

### **Rule 5301 – Effect of Sanctions**

Rule 5301 describes the effect of certain sanctions imposed by the Board. Rule 5301(a) applies to persons who have been suspended or barred from association with a registered public accounting firm or who have failed to comply with any other sanction imposed on them by the Board. Rule 5301 prohibits such persons from willfully becoming or remaining associated with any registered public accounting firm, unless they first obtain the consent of the Board, pursuant to Rule 5302, or of the Commission.

Rule 5301(b) applies to a registered public accounting firm. It prohibits a firm from permitting a person to become or remain associated with the firm if the firm knows, or in the exercise of reasonable care should have known, that the person is subject to a bar or suspension on such association, unless the firm first obtains the consent of the Board, pursuant to Rule 5302, or of the Commission.

With the proposed rules, the notes to Rule 5301(a) and Rule 5301(b) stated that the prohibition on association would prohibit the person from receiving, and the firm from paying or crediting, any salary, bonus, profit, or other remuneration that results directly or indirectly from any audit fees earned during the period of the suspension or

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bar. Several commenters suggested that there were significant practical obstacles to drawing the proposed line on compensation.

In response to those concerns, we have eliminated from each note the sentence that read, "[t]his prohibition includes receiving any salary, or any bonus, profit or other remuneration that results directly or indirectly from any audit fees, that might have been earned during the period of the suspension or bar." The relevant remaining portion of each note is an explanation rooted directly in the language of section 2(a)(9) of the Act, (which defines "associated person"): a person who is suspended or barred from being associated with a registered public accounting firm may not, "in connection with the preparation or issuance of any audit report . . . share[ ] in the profits of, or receive[ ] compensation in any other form from," any registered public accounting firm.

This language means two fundamental things. First, a barred or suspended person may not receive a share of the firm's profits from audit work. To the extent that any compensation is calculated as a share of profits – whether a partner's draw, or any other employee's bonus or other special compensation -- the calculation must be adjusted so that the portion of the firm's profits that is derived from audit revenue is not counted in calculating that compensation.

Second, a person may not be compensated in any form for doing audit work. This does not mean that a salaried employee must suffer a salary cut that mirrors the



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portion of the firm's profits that are from audit work, but it does reinforce the general prohibition on the person doing any audit work.

The language does not prohibit a barred partner from receiving from the firm a return of the partner's capital or a separation payment provided for in the partnership agreement. Nor does the language prohibit the payment of standard retirement benefits to which the person was entitled on the day the sanction took effect.

One commenter suggested that the rules prescribe at least one procedure which, if followed by a firm to determine whether a person is barred or suspended, would be "reasonable per se" and effectively provide a safe harbor for the firm from liability for associating with the person. The commenter suggested, as an example, that obtaining signed statements from individuals certifying that they are not suspended or barred could be a sufficient procedure for the firm to avoid liability.

We will continue to consider what, if any, sort of safe harbor procedure might be made available on this point. We reject the commenter's particular suggestion, however, simply because we see sufficient reason to be skeptical that persons who have committed transgressions serious enough to warrant bar or suspension will necessarily refrain from providing a false certification when seeking work. We would not consider mere reliance on such a certification reasonable. A bar or suspension, once it takes effect, will be a matter of public record, and the rule effectively requires that firms

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make reasonable efforts to confirm, through public records, that an individual is not barred or suspended. The Board will consider ways to make information about bars and suspensions more readily accessible to firms.

**Rule 5302 – Application for Relief from, or Modification of, Revocations and Bars**

Rule 5302 provides mechanisms by which a firm or person subject to a Board sanction may apply to the Board for relief from, or modification of, that sanction. Under Rule 5302(a), a firm that has had its registration revoked pursuant to a Board determination that permitted the firm an opportunity to reapply for registration after a specified period of time may, after the expiration of the specified period, file an application for registration pursuant to Rule 2101. The revocation shall continue, however, unless and until the Board affirmatively approves such a registration application.

Under Rule 5302(b), a person subject to a bar on association that contains a provision allowing the person to seek termination of the bar after a specified period of time may, after the expiration of the specified period, file a petition to terminate the bar. Subparagraphs (2) – (5) of Rule 5302(b) govern the process related to such a petition.

Commenters questioned the appropriateness of Rule 5302(b)(2)(iii)(D), which requires an individual who seeks relief from a bar to provide the Board with, among other things, the names of other associated persons, at the firm with which the



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individual seeks to associate, who have previously been barred by the Board or the Commission. Commenters stated that this information would not be readily available to the individual.

We have adopted the rule as we proposed it. While the requirements of the rule are framed with reference to the individual seeking relief from a bar, the burdens of the rule should not be viewed as falling solely on the individual. As a practical matter, the petition submitted by the individual should be a collaborative effort between the individual and the firm that wishes to associate with the individual. The firm should readily be able to supply the information necessary for the individual to satisfy the rule. The rule is based on Rule 193(b)(4)(iv) of the Commission's Rules of Practice, which imposes a similar requirement on barred individuals seeking to associate with a broker-dealer.

Rule 5302(c) governs modification of revocations and bars that do not expressly provide a time period after which the firm may reapply for registration or the person may petition to terminate the bar. Such firm or person may at any time request leave to reapply for registration or leave to file a petition to terminate a bar. They may not file a registration application or a petition to terminate the bar unless the Board grants such leave. The revocation and bar shall continue until the Board has both granted such leave and approved a subsequent application or petition.

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Under Rule 5302(d), a firm or person subject to an ongoing sanction imposed for noncooperation with an investigation may file an application for termination of that sanction once the firm or person has remedied the noncooperation that formed the basis for the sanction. The sanction shall continue, however, unless and until the Board orders it terminated.

One commenter suggested that the rules should include provisions governing a hearing for a person who applies for termination of an ongoing sanction. We see no need for special provisions on this point. A continuing sanction generally will be a matter that effectively remains within the jurisdiction of the Board, or the hearing officer, as a piece of the proceeding from which the sanction resulted. Any necessary hearing on termination of the sanction can be provided in that context, without the need to institute a new proceeding.

Under Rule 5302(e), any firm or person subject to a sanction described in subparagraphs (3), (6), (7), (8), (9), or (10) of Rule 5300(a) may file an application for termination of the sanction at any time. The Board may, in its discretion, grant a hearing on the application. The sanction shall continue, however, unless and until the Board orders it terminated.



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### **Rule 5303 – Use of Money Penalties**

Rule 5303 provides that all money penalties collected by the Board shall be used to fund a merit scholarship program as required by, and described in, Section 109(c)(2) of the Act.

### **Rule 5304 – Summary Suspension for Failure to Pay Money Penalties**

Under Rule 5304, the failure of a registered public accounting firm or an associated person to pay money penalties imposed by the Board may result in summary suspension, and effective revocation, of the firm's registration and summary suspension or bar from association. Under Rule 5304(a), if a firm fails to pay a money penalty after the exhaustion of all reviews and appeals and the termination of any stay, the Board may summarily suspend the firm's registration.

The proposed Rule 5304(a) required only that the Board provide the firm with written notice at least seven days before any such suspension. One commenter understood the proposal to mean that a firm or associated person might have only seven days between the date the sanction becomes final and the date of summary suspension under the rule. The commenter suggested that the rule provide for at least 30 days between the sanction becoming final and the Board sending the seven-day notice.

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The commenter's suggestion is consistent with what we intended by our proposal, and we have modified the rule to make that intent explicit. The rule that we adopt allows a thirty-day period for payment after a money penalty becomes final. If payment is not made in that thirty-day period, the Board may send a notice that failure to make payment within seven days will result in summary suspension.

Once such a suspension is imposed, it shall terminate upon payment of the penalty by the firm within 90 days of the onset of the suspension. If payment is not made within 90 days, the firm's registration will effectively be revoked, and the firm can re-register only by paying the penalty, plus interest, and filing an application for registration under Rule 2101 and obtaining Board approval of that application.

Under Rule 5304(b), if an associated person fails to pay a money penalty after exhaustion of all reviews and appeals and the termination of any stay, the Board may summarily suspend the person from association with a registered firm. Rule 5304(b) requires the Board to provide written notice at least seven days before any such suspension. As with Rule 5304(a), we have added to the final rule a provision allowing a thirty-day period for payment after a money penalty becomes final and before the Board may send the seven-day notice. Once a suspension is imposed, it shall terminate upon payment of the penalty, plus interest, within 90 days of the onset of the

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suspension. If payment is not made within 90 days, the Board may summarily bar the person from association with a registered firm.

#### **Part 4 – Rules of Board Procedure**

Part 4 of the Board's Rules on Investigations and Adjudications consists of Rules 5400 through 5469. These rules are further divided into general rules (5400 through 5411), prehearing rules (5420 through 5427), hearing rules (5440 through 5445), and appeals to the Board (5460 through 5469).

#### **Rule 5400 – Hearings**

Rule 5400 provides for hearings to be held only upon order of the Board and to be conducted in a fair, impartial, expeditious and orderly manner. The rule is adapted from Rule 200 of the Commission's Rules of Practice.

#### **Rule 5401 – Appearance and Practice Before the Board**

Rule 5401 provides that a person may appear on his own behalf before the Board or may be represented by counsel. Rule 5401 further provides that a member of a partnership may represent the partnership and a bona fide officer of a corporation, trust, or association may represent the corporation, trust, or association. Rule 5401(c) imposes certain procedural requirements related to representation and withdrawal.

Proposed Rule 5401(c)(4) provided that an individual's withdrawal from representation of a party would be permitted only with the approval of the Board or the

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hearing officer. One commenter suggested that it would be helpful if the rules would enumerate grounds that would be adequate for withdrawal. Other commenters suggested that the rules should provide that permission to withdraw would not be unreasonably withheld. One commenter suggested that a party's request to replace counsel (as distinct from counsel's request to withdraw) should not require approval.

We are sensitive to the importance of counsel being free to withdraw in appropriate circumstances, and the importance of a party being free to change counsel in appropriate circumstances. We are also mindful of the ways in which an ostensible desire to withdraw or to change counsel can be used to delay or disrupt proceedings. To provide some assurance of the limited scope within which we intend for the Board or hearing officer to withhold permission to withdraw, we have adopted the suggestion of those commenters who urged that the rule provide that permission to withdraw would not be unreasonably withheld.

#### **Rule 5402 – Hearing Officer Disqualification and Withdrawal**

Rule 5402 allows a party to make a motion for withdrawal of a hearing officer and governs the circumstances under which such a motion may be made and the time within which it must be made. Rule 5402 also provides for appointment of a replacement hearing officer in the event of withdrawal or disqualification. The rule is based on Rule 112 of the Commission's Rules of Practice and NASD Rule 9233.

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Commenters suggested that the rule should provide for a right of immediate interlocutory appeal to the Board from a hearing officer's denial of a recusal motion. One commenter stated that this was of particular importance given the possibility that Board staff, including enforcement staff, might be assigned to serve as hearing officers.

As discussed earlier, we have revised the definition of "hearing officer" to provide that neither a Board member nor any staff of the interested division will serve as a hearing officer. We decline to create a special right of interlocutory Board review in every case of a denied recusal motion. The interlocutory appeal process, governed by Rule 5461, allows a party to request that the hearing officer certify his or her recusal ruling for interlocutory review. The rule requires that the hearing officer should certify the ruling if immediate review of the order may materially advance the completion of the proceeding. Given that a reversible denial of a recusal motion could substantially delay completion of the proceeding by eventually requiring a complete re-hearing before a different hearing officer, we expect hearing officers to give careful attention to whether that standard for certification has been met with respect to any ruling denying a recusal motion.

One commenter suggested that the rule should provide that, if a hearing officer is replaced, the parties should have a right to move that certain testimony be reheard so that the new hearing officer may judge credibility. We believe that the rules as



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proposed and adopted are flexible enough to accommodate such a motion and to leave the decision within the discretion of the new hearing officer.

### **Rule 5403 – *Ex Parte* Communications**

Rule 5403 prohibits a hearing officer from having *ex parte* communications with a person or party, except to the extent permitted by law or by the Board's rules for the disposition of *ex parte* matters. The proposed rule also prohibited a party from having *ex parte* communication with the Board or any Board member on a fact in issue, except as permitted by law or by the Board's rules. Commenters suggested that the restriction should extend beyond the interested division to any Board staff that has had substantial involvement in a matter. We have revised Rule 5403(b) to impose the restriction not only on a party (including the interested division) but also on any Board staff that substantially assists the interested division on the particular matter, whether before or during the hearing,

The rule includes a specific exception allowing staff to discuss settlement offers with the Board when a party has provided the pre-judgment waiver described in Rule 5205(c)(3). The rule is based in part on Rule 120 of the Commission's Rules of Practice.

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**Rule 5404 – Service of Papers by Parties**

Rule 5404 requires service of papers on each party in a manner calculated to bring the paper to the attention of the party served. One commenter suggested that the rule be more specific, such as by requiring service by first class mail unless the hearing officer directs otherwise. We have adopted the rule as proposed. The rule is flexible enough to accommodate service by first class mail, or by other means, such as through electronic communication.

**Rule 5405 – Filing of Papers With the Board: Procedure**

Rule 5405 governs procedures for filing papers with the Board.

**Rule 5406 – Filing of Papers: Form**

Rule 5406 governs the form of papers to be filed with the Board.

**Rule 5407 – Filing of Papers: Signature Requirement and Effect**

Rule 5407 requires every paper filed to be signed either by the party, if the party represents himself or herself, or by counsel if the party is represented by counsel. Because the Board expects most papers to be filed electronically, a note to the rule states that the signature should be scanned into an electronic document where practicable, but that otherwise certain indicia of electronic signature will suffice.

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### **Rule 5408 – Motions**

Rule 5408 describes procedures and length limitations related to motions and supporting briefs. One commenter suggested that the time and page limits relating to motions are unduly restrictive. The commenter also suggested that the rules should give a hearing officer the authority to extend time periods, just as they give a hearing officer the authority to enlarge page limits. Rule 5408(b), as proposed and adopted, already provides the hearing officer with authority to extend time periods. In light of the flexibility given the Board and the hearing officer to adjust schedules and page limitations in appropriate circumstances, we decline to revise the rule to provide for longer time periods or larger page limitations generally.

### **Rule 5409 – Default and Motions to Set Aside Default**

Rule 5409 describes the circumstances that shall constitute a default and the procedure for seeking to set aside a default. The rule is adapted from Rule 155 of the Commission's Rules of Practice.

### **Rule 5410 – Extra Time for Service by Mail**

Proposed Rule 5410 included paragraph (a), concerning time computation, and paragraph (b), concerning additional time for service by mail. As noted above in connection with Rule 1002, we have adopted the substance of paragraph (a) but we have moved it to part I of the rules in order to give it broader application. We have

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adopted the substance of proposed paragraph (b), providing an additional three days for service made by mail, as Rule 5410.

**Rule 5411 – Modifications of Time, Postponements and Adjournments**

Rule 5411 provides that the Board maintains discretion, except as otherwise provided by law, to adjust the time limits prescribed by the rules or to postpone or adjourn any hearing.

**Rule 5420 – Leave to Participate to Request a Stay**

Rule 5420 provides a procedure by which certain entities may seek a stay of a hearing. Under the proposed rule, the entities that may seek such a stay would have been the Commission, the United States Department of Justice or any United States Attorney's Office, and any criminal prosecutorial authority of a state or political subdivision of a state. One commenter suggested that the list should be expanded to include an appropriate state regulatory authority. We agree with that comment and have modified the rule accordingly.

Under Rule 5420, an authorized representative of any such entity may seek leave to participate on a limited basis to request a stay. Rule 5420 provides that a stay shall be granted upon a showing that a stay is necessary to protect an ongoing Commission investigation, and that a stay shall otherwise be favored upon a showing that it is in the public interest or for the protection of investors.

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One commenter suggested that the rule should require that any person who appears in order to seek a stay must maintain the confidentiality of information in those proceedings. We have not adopted this suggestion. The entities that may participate under this rule are regulatory or criminal prosecutorial authorities. We do not believe the public interest is served by imposing any obstacle to or condition on their making a formal request that Board proceedings be stayed in the interest of ongoing regulatory or criminal investigative or other proceedings. Moreover, even before participating to seek a stay, some of them will already have received information from the Board pursuant to section 105(b)(5)(B) of the Act, subject to that section's confidentiality requirement. Appearing for the purpose of requesting a stay will not afford them access to information beyond what they may have received under section 105(b)(5)(B) unless a respondent, in opposing the stay request, chooses to provide more information. In any event, the request to participate, and the request for a stay, will also be nonpublic.

#### **Rule 5421 – Answer to Allegations**

Rule 5421 governs the filing of answers to orders instituting proceedings. A party may file an answer in any matter, but is not required to file an answer unless ordered to do so in the order instituting proceedings.

Commenters suggested that the rule should provide 21 days, rather than five days, for a respondent to file an answer in a noncooperation proceeding. We agree that

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a strict five-day rule is not appropriate, given that some noncooperation proceedings may involve complex issues. We also believe that a general 21-day rule would be inappropriate in many uncomplicated matters of noncooperation. We have modified the rule to require an answer in a noncooperation proceeding within five days as a general matter, but to allow the hearing officer and the Board discretion to allow a longer period.

#### **Rule 5422 – Availability of Documents for Inspection and Copying**

Rule 5422 governs the obligations of Board staff to make documents available to a party for inspection and copying. Under the rule, the staff's obligation varies according to whether the proceeding is commenced under Rule 5200(a)(1)-(2) for violations or failures reasonably to supervise, Rule 5200(a)(3) for noncooperation, or Rule 5500 concerning disapproval of a registration application. In response to comments, we have made several changes to Rule 5422. In particular, we have revised the structure of the rule in response to commenters' suggestions that the rule should more closely track the Commission's approach with respect to so-called Brady material. We have added provisions to reinforce the principle that material exculpatory evidence will not be withheld even if the confidential informant privilege or other good cause would otherwise justify withholding it. We have also modified the rule to provide that documents made available in a noncooperation proceeding will include any documents that contain material exculpatory evidence on the issue of noncooperation.

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Finally, we have revised the rule to require the Division to provide a privilege log with respect to a certain category of documents. We now turn to a description of the rule as we have adopted it.

Paragraphs (a) through (c) of Rule 5422 are the core provisions for determining what documents the staff must make available. Paragraph (a) describes generally the documents that the staff must make available to a respondent. Paragraph (b) limits paragraph (a) by describing categories of documents that the staff may withhold, subject to an overriding obligation not to withhold material exculpatory evidence. Paragraph (c) prescribes procedures the staff must follow when withholding certain categories of documents, and procedures for a hearing officer to determine whether withholding is appropriate.

Rule 5422(a)(1) applies to proceedings commenced under Rule 5200(a)(1) or Rule 5200(a)(2). The rule provides that in those proceedings, the Division of Enforcement and Investigations shall make available all documents in four specific categories: (1) accounting board requests, subpoenas, and accounting board demands for documents, testimony, or information issued in the investigation or in the informal inquiry, if any, that preceded the investigation, (2) responses to those accounting board requests, subpoenas, and accounting board demands, including any documents produced in response, (3) testimony transcripts and exhibits, and any other verbatim

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records of witness statements, and (4) all other documents prepared or obtained by the Division of Enforcement and Investigations in connection with the investigation prior to the institution of proceedings.

Rule 5422(a)(2) applies to noncooperation proceedings commenced under Rule 5200(a)(3). Rule 5422(a)(2) requires that the Division of Enforcement and Investigations make available all documents on which the Division intends to rely in seeking a finding of noncooperation. The rule expressly provides that the Division shall not be required to make available any other documents in a proceeding based on noncooperation, subject only to the general requirement to make available material exculpatory evidence on the issue of noncooperation.

One commenter suggested that the rule should require disclosure of all documents "relevant" to the noncooperation proceeding, rather than just documents on which the staff intends to rely. As discussed below, we have added a requirement that the staff also provide any documents that contain material exculpatory evidence on the issue of noncooperation. We decline to expand the production obligation further. We anticipate that noncooperation proceedings will narrowly focus on such things as, for example, the demand with which there has been no compliance, or the testimony that is allegedly false. The only documents that would be relevant in those examples are the documents that the Division would use to prove noncooperation and any documents

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that would tend to show that the person did comply with the demand, or that that person's testimony was not false. Under the rule that we adopt, all such documents must be made available to the respondent in a noncooperation proceeding.

We decline, however, to adopt a "relevance" standard and open the door to broader disputes about what documents might be "relevant." Liability for noncooperation is independent of whether the party has otherwise violated any law, rule, or standard enforceable by the Board. Noncooperation is not excusable on the basis of a conviction that the staff's investigation is misguided. We do not intend for noncooperation proceedings to become a forum for demonstrating, through broad access to the investigative record, that the investigation is flawed and that something less than full cooperation was therefore justified. A noncooperation proceeding focuses only on the obligation to cooperate, which is not a qualified obligation that varies depending upon one's view of the merits of the investigation.

Moreover, as we stated in proposing the rules, we intend that noncooperation proceedings will generally be commenced as soon as the grounds for such a proceeding appear, rather than waiting until the conclusion of an investigation.<sup>8/</sup> An

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<sup>8/</sup> The rules do not preclude the Board from commencing a proceeding for noncooperation after an investigation and prosecuting it separately from or consolidated with a proceeding for alleged violations of laws, rules, or standards enforceable by the Board. For example, the Board may, in its discretion, institute proceedings for violations of the Act and simultaneously institute proceedings for noncooperation in an

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important objective of a noncooperation proceeding will be not only to impose a sanction if appropriate, but also to compel the cooperation at a time when it is still meaningful to the investigation. At that point in time, to require the staff to make available any portion of the investigative record other than that directly bearing on noncooperation could compromise the investigation, and might also compromise investigations by the Commission or other authorities. Indeed, to allow access to any portion of the investigative record in the course of a noncooperation proceeding would supply a counterproductive incentive that might cause some persons to fail to cooperate specifically for the purpose of obtaining access to that record.

Rule 5422(a)(3) applies to registration disapproval proceedings commenced pursuant to Rule 5500. Rule 5422(a)(3) requires the Division of Registration and Inspections to make available all documents obtained by the Division in connection with the registration application prior to the notice of hearing.

Rule 5422(a) includes specific exceptions for, and must be read in conjunction with, Rule 5422(b), which describes four categories of documents that the Division may withhold from a respondent even if Rule 5422(a) would otherwise require the Division to make the document available. Moreover, withholding documents may trigger the procedural requirements of Rule 5422(c). We therefore individually address each of the

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investigation against the same respondent for conduct (for example, false testimony) during the investigation.



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four categories of documents that may be withheld under Rule 5422(b), and any Rule 5422(c) procedures related to withholding those documents.

Under Rule 5422(b)(1)(i), the Division need not make available any document prepared by a member of the Board or the Board's staff that has not been disclosed to any person other than Board members, Board staff, or persons retained by the Board or Board staff to provide services in connection with the investigation, disciplinary proceeding, or hearing on disapproval of registration. Withholding such documents does not trigger any procedural requirements under Rule 5422(c). Commenters generally expressed two concerns about this category of documents. They suggested that the rules should require the staff to supply a log of the documents, and they suggested that a respondent should be entitled to review every document reviewed by a Board official who may ultimately participate in deciding the case.

We do not adopt the privilege log suggestion as to this category of documents. The privileged and confidential nature of the documents described in paragraph (b)(1)(i) would be clear enough even in the absence of section 105(b)(5)(A) of the Act, but section 105(b)(5)(A) eliminates any question about the Board's authority to maintain this category of documents in confidence even after commencing a proceeding. We decline to require the staff to create a log for these documents when there exists no reasonable basis on which a respondent might contest the decision to withhold.

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Nor do we adopt the suggestion that a respondent should have the chance to review every document that the staff shows to the Board. Again, this is inconsistent with the confidentiality and privilege protection supplied by section 105(b)(5)(A). Moreover, although the commenters perceive some unfairness on this point, even federal agencies operating under the fairness constraints imposed by the Administrative Procedure Act routinely engage in the practice of receiving confidential advice from their staff, including investigative staff, up to the point in time when the agency authorizes an enforcement proceeding. It is only after that point that rules on ex parte communications constrain the agency's contact with its staff. We do not perceive similar line-drawing to be any less fair in the context of our proceedings than in the context of federal agency proceedings.

Under Rule 5422(b)(1)(ii), the Division need not make available any other document that, while not encompassed within the first category, is nevertheless protected by a privilege or by the attorney work product doctrine. This category would include, for example, documents that were privileged in the hands of the person who supplied them to the Board, but who supplied them pursuant to an understanding that doing so would not otherwise waive the privilege. As to this category of withheld documents, Rule 5422(c)(1) requires the Division to supply to the hearing officer and

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each respondent a log providing all of the same information that Rule 5106 requires a person to submit when asserting a privilege against production to the Board.

Under Rule 5422(b)(1)(iii), the Division need not make available any document that would disclose the identity of a confidential source. We have declined to narrow this provision in response to commenters who suggested that its application should be limited to the same scope as the common law confidential informant privilege. We have, however, specifically provided that the staff may not withhold a document on this basis if doing so results in withholding material exculpatory evidence. Rule 5422(c)(2) requires the Division to provide the hearing officer with a list of any documents withheld to protect the identity of a confidential informant. The rule requires the Division to provide the same list to each respondent, although the staff may redact as much information as necessary from that list (including, in appropriate circumstances, all information) to protect the interests related to the Division's reason for withholding the document. The hearing officer, in his or her discretion, may review any such document in camera to assess the grounds for withholding it and to assess whether it includes material exculpatory evidence.

Under Rule 5422(b)(1)(iv), the Division need not make available any other document that the staff identifies for the hearing officer's consideration as to whether the document may be withheld as not relevant to the subject matter of the proceeding or

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otherwise for good cause shown. Commenters expressed concern that "good cause" was too indefinite a standard. We believe, however, that some general exception is necessary for categories of documents that the staff may occasionally have but may not intend to use as evidence. For example, the staff might have documents supplied by a foreign regulator under a confidentiality agreement. If the staff does not intend to use them, the "good cause" exception allows the staff to withhold them to honor the confidentiality agreement. Again, however, the good cause exception does not allow the staff to withhold a document that contains material exculpatory evidence. Rule 5422(c)'s procedures, described above with respect to confidential informant documents, apply in the same fashion to documents withheld as irrelevant or otherwise for good cause.

In addition to the procedural protections described above, Rule 5422(b)(2) provides an over-arching Brady-type restriction on what the Division may withhold. It provides that nothing in paragraph (b), and nothing in paragraph (a)(2)'s limitation on what the staff must make available in a noncooperation proceeding, authorizes the interested division to withhold documents that contain material exculpatory evidence.

Rule 5422(d) governs the time period in which the staff must make the documents available. Under the rule, the staff must make the documents available within seven days of the institution of a proceeding under Rule 5200(a)(3) for



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noncooperation, and within 14 days of the institution of proceedings under Rules 5200(a)(1), 5200(a)(2), and 5500. In response to a comment, a technical correction to the rule makes clear that the prescribed time period indicates the deadline by which all documents must be available to the respondent.

Rule 5422(e) provides that the staff shall make the documents available at the Board's office where the documents are normally maintained, or at such other place as the parties agree upon in writing. Rule 5422(d) further provides that, except as subject to any specific contrary agreement with the staff, a party shall not have custody of the documents and shall not remove the documents from the Board's offices, though the party may make and retain copies of the documents. Rule 5422(f) provides that a party wishing to make copies of the documents must bear the cost of copying.

Rule 5422(g) addresses any failure by the interested division to make available any document that these rules required it to make available. The rule provides that, in that event, no person shall be entitled to a rehearing or redecision in a matter already heard or decided unless that person first establishes that the failure to make the document available did not constitute harmless error.

A note following Rule 5422 points out that the obligations of the interested division under this rule extend only to documents obtained by that division, and that this Rule does not require the interested division to make available documents located only

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in the files of other divisions or offices. The proviso, however, is not intended to relieve the interested division of the obligation to make available any such document that the division knows of and intends to introduce as evidence. Any such document should be treated, for purposes of Rule 5422, just as if it were physically located in the division's files.

#### **Rule 5423 – Production of Witness Statements**

Rule 5423(a) provides that a respondent may move that the interested division produce any statement of a person, called or to be called as a witness by the division, that pertains or is expected to pertain to his or her direct testimony and that would be required to be produced pursuant to the Jencks Act, 18 U.S.C. § 3500, if the Board were a governmental entity. The hearing officer shall have authority to grant such a motion and require production of any such statement. Rule 5423(b) provides, however, that the interested division's failure to produce any such statement shall not be grounds for rehearing or redetermination of a matter already heard or decided unless the respondent first establishes that the failure to produce the statement was not harmless error. The rule is based on Rule 231 of the Commission's Rules of Practice.

#### **Rule 5424 – Accounting Board Demands and Commission Subpoenas**

Rule 5424 provides for mechanisms by which any party may seek to secure testimony or evidence relevant to a proceeding. Rule 5424(a) describes procedures by



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which any party may seek to have an accounting board demand served on any registered public accounting firm or associated person of such a firm, or seek to have an accounting board request served on any other person. Under the rule, the party must make a request to the hearing officer for issuance of the accounting board demand or accounting board request. In the event of the hearing officer's unavailability, the party may present its request, through the Secretary, to any member of the Board, or any other person designated by the Board to issue such demands and requests.

The application for an accounting board demand or accounting board request may be denied, or may be granted with modifications, if it is unreasonable, oppressive, excessive in scope, or unduly burdensome. The rule provides that a person whose application for an accounting board demand or accounting board request has been denied or modified may not make the same application to another person and may not apply to the Board for a Commission subpoena covering the same testimony, documents, or information as the denied application covered or as was excluded by modification in granting an application. Rule 5424(a) also provides that a party who applies for an accounting board demand or accounting board request to summon a witness shall pay the witness's reasonable expenses.

Rule 5424(b) provides that the Board, on its own initiative or on the application of any party, may seek issuance of a subpoena by the Commission to any person in order

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to seek to secure testimony or evidence that the Board considers relevant or material to the proceeding. Unlike Rule 5424(a), which provides that an application for an accounting board demand or request shall be granted if certain criteria are satisfied, Rule 5424(b) leaves entirely to the discretion of the hearing officer or other Board designee whether to grant a party's request to seek a Commission subpoena. The rule does not create any entitlement, under any circumstances, to have the Board seek a Commission subpoena on behalf of a party. Moreover, if the Board does seek a Commission subpoena requested by a party, the rule does not, and should not be understood to, give rise to or justify any expectation about how or whether the Commission will respond to the request. Accordingly, the rule does not create any entitlement to have any Board proceedings stayed or delayed while any such request is pending.

Two commenters suggested that the rules should provide for a broader discovery process to address what they perceive to be an imbalance that works against the respondent. We are not persuaded that there is a meaningful imbalance. Virtually from the outset of the proceeding, the respondent has access to the evidentiary record compiled by the Division during the investigation. The respondent has access to all of the information in the documents and to the transcripts showing what testimony witnesses have provided in response to questions put to them. The Division and the

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respondent are equally unenlightened as to what may exist in any other documents and as to what testimony witnesses would give in response to questions not yet put to them. The Division and the respondent have the same opportunity to seek board demands, board requests, or Commission subpoenas, and the same opportunity to interview prospective witnesses. The provisions of the rule are fair and are consistent with discovery provisions in administrative proceedings in other contexts.

In response to comments, we have made technical corrections to Rule 5424. We have used the word "party" in place of the less precise terms "person" and "applicant."

#### **Rule 5425 – Depositions to Preserve Testimony for Hearing**

Rule 5425 provides procedures by which a party may seek a deposition for the purpose of preserving for a hearing the testimony of a person who may be unavailable to appear at the hearing. Rule 5425 does not provide for depositions taken for the purpose of discovery. The rule is adapted from Rule 233 of the Commission's Rules of Practice.

Under Rule 5425(a), a party seeking to take a deposition to preserve testimony must make a written motion setting out the reasons why the deposition is necessary and specifically including the reasons that the party believes the witness will be unable to testify at the hearing. The motion must also identify the witness, the matters on which the party intends to question the witness, and the proposed time and place of the

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deposition. Under Rule 5425(b), the hearing officer may grant the motion if the hearing officer finds that the witness will likely give testimony material to the proceeding, that it is likely the witness will be unable to appear at the hearing because of age, sickness, infirmity, imprisonment or other disability, or will otherwise be unavailable, and that the taking of the deposition will serve the interests of justice. Rules 5425(c)-(e) describe certain procedures governing any such deposition allowed by the hearing officer. In response to comments, we have made a technical correction eliminating references to the concept of a "deposition officer."

#### **Rule 5426 – Prior Sworn Statements of Witnesses in Lieu of Live Testimony**

Rule 5426 provides procedures by which a party may introduce into evidence a witness's prior sworn statement in lieu of live testimony by the witness. Rule 5426 is not a limitation on any party's ability to introduce a prior sworn statement with respect to a witness who appears in person and testifies (for purposes of impeachment, for example). But Rule 5426 does limit the circumstances in which a party may introduce a prior sworn statement in lieu of live testimony by the witness.

Rule 5426 identifies five circumstances in which the hearing officer may grant a motion to introduce a prior sworn statement in lieu of live testimony: (1) if the witness is dead, (2) if the witness is outside of the United States, unless it appears that the witness's absence from the country was procured by the party offering the prior sworn

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statement, (3) if the witness is unable to attend because of age, sickness, infirmity, imprisonment or other disability, (4) if the party offering the prior sworn statement has been unable to procure the attendance of the witness by accounting board demand, or (5) if, in the discretion of the Board or the hearing officer, it would be desirable, in the interests of justice, to allow the prior sworn statement to be used. In granting a motion to introduce a prior sworn statement, a hearing officer has the discretion, under Rule 5426, to require that all relevant portions of the statement be included or to exclude portions of the statement not relevant to the proceeding.

#### **Rule 5427 – Motion for Summary Disposition**

Rule 5427 provides for any party to make a motion for summary disposition. Under Rule 5427(a), the interested division may make such a motion only after the party against whom the motion is directed has filed an answer and has had documents made available to it pursuant to Rule 5422. Under Rule 5427(b), a respondent may make such a motion at any time.

Rule 5427(c) requires that any party that would move for summary disposition must first request and attend a pre-motion conference with the hearing officer. Under the rule, the hearing officer would, at the conference, set a due date for the motion. The hearing officer has discretion either to set a due date for a response to the motion or to spare the opposing party the need to prepare a response until the hearing officer has

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reviewed the motion. If the hearing officer chooses that approach, the hearing officer shall review the motion and then either deny the motion without any response being filed or shall give the opposing party an opportunity to file a response.

Rule 5427(d) provides that a hearing officer shall grant a motion for summary disposition if the pleadings, depositions, and admissions on file, together with any affidavits, show that there is no genuine issue as to any material fact and that the moving party is entitled to a disposition as a matter of law. A hearing officer may also enter a summary disposition that is limited to the issue of liability even though there may be a genuine and contested issue as to the appropriate sanction. Rule 5427(d) also provides that the denial of a motion for summary disposition is not subject to interlocutory appeal. Rule 5427(e) governs page limitations on briefs related to motions for summary disposition.

Two commenters questioned whether summary disposition could ever be appropriate for a disciplinary proceeding, particularly given what the commenters perceive to be inequitable discovery provisions. By the time of any summary disposition motion, however, a respondent would have access to the full evidentiary record available to the Division. The fact that one side was responsible for compiling that evidentiary record does not make it any more or less likely that the compiled evidence demonstrates the absence of any genuine issue as to any material fact. The standard

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for summary disposition is high, and a motion is usually defeated by, for example, affidavit evidence that indicates conflicting factual evidence that might only be resolved by judging the credibility of witnesses subjected to cross-examination. We have adopted the rule as we proposed it.

### **Rule 5440 – Record of Hearings**

Rule 5440 describes procedures related to the creation, correction, and availability of hearing transcripts.

### **Rule 5441 – Evidence: Admissibility**

Rule 5441 provides that a hearing officer may receive relevant evidence and shall exclude all evidence that is irrelevant, immaterial or unduly repetitious. One commenter urged the Board to adopt greater structure for its evidentiary rules. The commenter noted that the rule appeared to leave out basic grounds for the exclusion of evidence recognized in the Federal Rules of Evidence, and argued that discretion in the hearing officer is inappropriate in proceedings that have the serious consequences of Board disciplinary proceedings.

After considering this comment, the Board has decided to adopt the rule as proposed. The standard in Rule 5441 is based on the Administrative Procedures Act.<sup>9/</sup>

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<sup>9/</sup> 5 U.S.C. 556(c)(3) and (d).



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In addition, the same standard is used in the SEC's Rules of Practice.<sup>10/</sup> By using this phrase in Rule 5441, the Board intends for evidentiary issues in PCAOB hearings to be addressed in a generally similar manner to SEC administrative hearings, and the administrative hearings of most other administrative agencies. Rule 5441 is not intended to limit a hearing officer's authority to exclude or allow evidence based on reasonable principles of admissibility, but is intended to allow a hearing officer reasonable flexibility.<sup>11/</sup> In particular, the three bases in the rule -- irrelevance, immateriality, and undue repetition -- are not the only permissible bases on which a hearing officer may exclude evidence under administrative practice. Nor does the standard in Rule 5441 preclude a hearing officer from referring to principles from the Federal Rules of Evidence or other authoritative sources in exercising his or her discretion to resolve evidentiary issues.<sup>12/</sup>

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<sup>10/</sup> See SEC Rule of Practice 320, 17 C.F.R. § 201.320 ("The Commission or the hearing officer may receive relevant evidence and shall exclude all evidence that is irrelevant, immaterial or unduly repetitious.")

<sup>11/</sup> See, e.g., Commission Opinion: Wheat, First Securities, Inc.; Rel. No. 34-48378, (August 20, 2003) (holding that hearsay is admissible in an SEC administrative hearing, but noting that the "record shows the probative and reliable nature of this evidence").

<sup>12/</sup> See *id.* (explaining that same result would have been reached had the administrative law judge applied the Federal Rules of Evidence).

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**Rule 5442 – Evidence: Objections and Offers of Proof**

Rule 5442(a) provides that any objections must be made on the record and must be in short form, stating the grounds relied upon. Under Rule 5442(a) any exception to a hearing officer's ruling on an objection need not be noted at the time of the ruling but will be deemed waived on appeal to the Board unless the exception was raised (1) on interlocutory review under Rule 5461, (2) in a proposed finding or conclusion filed under Rule 5445, or (3) in a petition for Board review of an initial decision filed under Rule 5460. Rule 5442(b) provides that when evidence is excluded from the record, the party offering the evidence may make an offer of proof which shall be included in the record. The excluded material itself would be retained under Rule 5202(b).

**Rule 5443 – Evidence: Presentation Under Oath or Affirmation**

Rule 5443 provides that witnesses at a hearing shall testify under oath or affirmation.

**Rule 5444 – Evidence: Rebuttal and Cross-Examination**

Rule 5444 provides that a party may present its case or defense by oral or documentary evidence, submit rebuttal evidence, and conduct such cross-examination as, in the discretion of the Board or the hearing officer, may be required for a full and true disclosure of the facts. The rule provides that the Board or hearing officer shall determine the scope and form of evidence, rebuttal evidence, and cross-examination in



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any proceeding. The rule is adapted from Rule 326 of the Commission's Rules of Practice.

### **Rule 5445 – Post-hearing Briefs and Other Submissions**

Rule 5445 provides procedures relating to the submission of post-hearing briefs and other submissions.

### **Rule 5460 – Board Review of Determinations of Hearing Officers**

Rule 5460 concerns Board review of initial decisions. Under Rule 5460, a party may obtain Board review of an initial decision by filing a timely petition setting forth specific findings and conclusions of the initial decision to which the party takes exception and setting forth the supporting reasons for each exception. To be timely, a petition must be filed within 10 days of an initial decision in a proceeding commenced under Rule 5200(a)(3) for noncooperation, and within 30 days of an initial decision in other proceedings. The rule is based in part on Rule 410 of the Commission's Rules of Practice.

Also under Rule 5460(a), if one party submits a timely petition for review, any other party then has an additional ten days to submit its own petition for review, even if its petition raises different issues than those raised by the first party to submit a petition. The purpose of this rule is to avoid the unnecessary expenditure of Board resources in cases where no party would appeal if it knew that the other party would not appeal, but

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in which one or more parties nevertheless appeal because of a concern that failing to appeal will deprive it of the opportunity to raise its issues in any appeal lodged by another party. Under Rule 5460(a), no party need guess about the other party's intentions, and no party sacrifices anything by waiting to see whether another party files a timely petition for review.

Rule 5460(b) provides that the Board may, on its own initiative, order review of all or any portion of an initial decision even if no party seeks review. The Board may order such review, however, only if it does so before the initial decision would otherwise become the final decision of the Board pursuant to the operation of Rule 5204(c). In effect, this allows the Board to order review on its own initiative for a period of 20 days beyond the deadline for a party to petition for review. The rule is based in part on Rule 411 of the Commission's Rules of Practice. Rules 5460(c)-(e) set out procedural matters related to Board review.

### **Rule 5461 – Interlocutory Review**

Rule 5461 concerns Board interlocutory review of hearing officer rulings. Under Rule 5461(a), the Board will not grant interlocutory review absent extraordinary circumstances, but also may direct at any time that any matter or ruling be submitted to the Board for review. Rule 5461(b) provides that a hearing officer shall certify a ruling for interlocutory review only if (1) the ruling would compel testimony of Board members,

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officers or employees or the production of documentary evidence in their custody, or (2) the ruling involves a controlling question of law as to which there is substantial ground for difference of opinion and immediate review of the order may materially advance completion of the proceeding. Rule 5461(c) provides that neither an application for, nor the granting of, interlocutory review shall stay the proceeding unless otherwise ordered by the hearing officer or the Board. The rule is adapted from Rule 400 of the Commission's Rules of Practice and 28 U.S.C. § 1292(b).

### **Rule 5462 – Briefs Filed with the Board**

Rule 5462 describes procedural requirements related to briefs and the filing of briefs. The rule is adapted from Rule 450 of the Commission's Rules of Practice.

### **Rule 5463 – Oral Argument Before the Board**

Rule 5463 concerns oral argument before the Board. Under Rule 5463(a), the Board may order oral argument, with or without the motion of a party, on any matter. The rule provides that, in general, motions for oral argument will be granted unless exceptional circumstances make oral argument impractical or inadvisable. Rules 5463(b)-(c) provide for procedures relating to oral argument. Rule 5463(d) provides that a member of the Board who is not present for oral argument may nevertheless participate in the Board's decision as long as the Board member reviews a transcript of the argument before participating in the decision.



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One commenter asked for clarification on whether the rule only permitted a request for oral argument to be made by the first party to submit a brief. The rule provides that any party may request oral argument, but the party must do so in its initial brief on the merits.

#### **Rule 5464 – Additional Evidence**

Rule 5464 provides that the Board may, upon its own motion or the motion of a party, allow the submission of additional evidence in connection with the Board's review of an initial decision. The rule is adapted from Rule 452 of the Commission's Rules of Practice.

#### **Rule 5465 – Record Before the Board**

Rule 5465 provides that the Board shall determine each matter on the basis of the record and provides certain requirements concerning the record. The rule is adapted from Rule 460 of the Commission's Rules of Practice.

#### **Rule 5466 – Reconsideration**

Rule 5466 provides procedures by which a party may seek reconsideration of a Board decision. The rule is adapted from Rule 470 of the Commission's Rules of Practice.

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**Rule 5467 – Receipt of Petitions for Commission or Judicial Review**

Rule 5467 is intended to ensure that the Board has notice of any petitions filed by a party for review of a Board decision, or for review of a Commission order with respect to a Board decision. Rule 5467 is separate from, and in addition to, any notice or service requirements that the Commission imposes with respect to petitions for review filed with the Commission. Rule 5467, a registered public accounting firm must notify the Secretary, or any requirements of the Federal Rules of Appellate Procedure or any court within 10 days after the firm or any person associated with the firm files with the Commission a petition for review of a Board decision or files a petition for court review of a Commission order with respect to such a sanction. The rule is modeled in part on Rule 490 of the Commission's Rules of Practice.

One commenter suggested that, as to petitions filed by associated persons, the rule should put the burden on the associated person to report to the Board and should also require the associated person to notify the firm. We have not changed the rule in response to these comments.

A firm will generally have in place a mechanism for regular reporting to the Board, and the Board will have in place a mechanism for receiving reports from a firm. These things generally will not be true with respect to individuals who are associated persons. The rule imposes no unfair burden on the firm. An associated person who is



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in the position of petitioning for review of a sanction is a person who, necessarily, has been sanctioned. That sanction, and whether it becomes final by virtue of an appeal period running without the person having petitioned for review, is something that the firm must necessarily monitor since it affects how the firm may or must interact with the associated person. Accordingly, we expect the firm as a matter of course to know whether and when its associated person has petitioned for review, and there is no unfair burden in requiring the firm to report that fact to the Board. We leave to the firm the creation and enforcement of internal procedures to ensure that its associated persons report the information to the firm.

We have, however, modified Rule 5467 to eliminate a possible ambiguity. The rule now expressly provides that a firm's obligation to report concerning an associated person does not extend to a person that is primarily associated with another registered public accounting firm.

#### **Rule 5468 – Appeal of Actions Made Pursuant to Delegated Authority**

As directed by Section 101(g)(2) of the Act, Rule 5468 provides procedures for seeking Board review of any action by someone other than the Board pursuant to authority delegated by the Board.

One commenter suggested that five days is too short a period within which to seek review of staff action pursuant to delegated authority. The proposed rule,



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however, did not require a petition for review to be filed within five days. The proposed rule, and the rule we adopt, require a person to act within five days to provide notice to the Board that the person intends to seek review. The rule allows the person another five days beyond that notice in which to submit the petition for review.

We have tried to clarify this point by rephrasing the first sentence of Rule 5468(a) in terms of a "person intending to seek" review, rather than in terms of a "petition for" review. We have also added a provision to Rule 5468(a) designed to ensure that a person will not unfairly be denied an opportunity to petition for review if, through no fault of the person, service of notice of the staff action in question was delayed in reaching them.

**Rule 5469 – Board Consideration of Actions Made Pursuant to Delegated Authority**

Rule 5469 provides procedures relating to Board consideration of petitions for review of actions made pursuant to authority delegated by the Board. We have made two changes to Rule 5469 from the rule as proposed. First, we have made clear, in rule 5469(a), that the Board may act summarily on the basis of the petition, or on the basis of the petition and any staff response, or may require additional statements in support of or opposition to the petition. Second, we have eliminated the provision of Rule 5469(b) that provided that the effect of any staff action would be stayed pending any petition for



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review of that action. We believe it is more appropriate that the effect of staff action not be stayed unless specifically ordered by the Board.

### **Part 5 – Hearings on Disapproval of Registration Applications**

Part 5 of the Board's Rules on Investigations and Adjudications consists of Rules 5500 and 5501. These rules relate to adjudications on certain registration applications.

#### **Rule 5500 – Commencement of Hearing on Disapproval of a Registration Application**

Rule 5500 describes the procedure relating to the commencement of a Board adjudication proceeding to consider an application for registration. Under the Board's registration rules, if the Board is unable to make the determination necessary to approve a registration application, the Board will provide the applicant with notice of a hearing. Rule 5500 provides the procedures through which such a proceeding would be commenced.

Specifically, Rule 5500 provides that a proceeding would commence after the Board provides a notice of hearing under Rule 2106(b)(2)(ii) and the applicant timely files a request for a hearing date and notice of appearance, rather than opting to treat the Board's notice of hearing as a denial of the application. Under Rule 5500(b), a request for hearing must include a statement that the applicant has elected not to treat the notice of hearing as a disapproval of its application and a statement describing with



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specificity why the applicant believes that the Board should not disapprove the application.

**Rule 5501 – Procedures for a Hearing on Disapproval of a Registration Application**

Rule 5501 provides that proceedings commenced pursuant to Rule 5500 are subject to the procedures set out in Parts 2 and 4 of Section 5 of the Board's rules.