

# Accounting Law Bulletin

## PCAOB Adopts Reporting Requirements for Registered Accounting Firms

Section 102(d) of the Sarbanes-Oxley Act of 2002 provides that registered public accounting firms are required to submit an annual report to the Public Company Accounting Oversight Board ("PCAOB"), and may also be required to report more frequently information specified by the PCAOB or the Securities and Exchange Commission (SEC). Until now, the PCAOB required only the initial registration of accounting firms, and had not implemented a requirement for annual reports or amendments to report material changes in the initial registration information. The purposes of the new rules are (i) to keep the PCAOB informed as to a firm's basic professional information, (ii) to provide the PCAOB with current information regarding a firm's audit practice in order to facilitate analysis and inspection by the PCAOB, and (iii) to alert the PCAOB as to the occurrence of any events that would require more immediate action by the PCAOB or that might warrant public disclosure.

On June 10, 2008, the PCAOB amended five existing rules and adopted eight new rules and two new forms to implement statutory reporting requirements. The amendments, new rules and forms require registered accounting firms to provide current information necessary or appropriate for the public interest and investor protection. The new reporting requirements become effective 60 days after the SEC approves the new rules.

### *Initial Registration*

An accounting firm's initial report is filed with the PCAOB on Form 1 and is required before an accounting firm is allowed to attest to financial statements being filed by an issuer with the Commission. Form 1 must be submitted through the PCAOB's web-based registration system. The PCAOB has 45 days to take action after the firm submits its application. There are three possible actions: approval, issuance of a notice of a hearing, or request for additional information. If the PCAOB

requests additional information concerning the application, a new 45-day period will begin when the additional information is received. The new rules do not alter the information required in the Form 1 registration.

### *Annual Report*

The PCAOB adopted the new Form 2 for annual reporting by registered accounting firms. Its purpose is to provide a profile of the firm at a point in time based on its activity related to issuers over the most recent 12-month period. Form 2 requires the firm to provide, among other things, information about the firm's public issuer-related practice, internal and external resources on which the firm draws in performing audits, certain new relationships and acquisitions, and an affirmation related to the firm's statutory obligations to cooperate with the PCAOB.

The significant reporting elements on Form 2 for the 12-month reporting period include the following:

- out of all fees billed by the firm to all clients for all services, the percentages of such fees that were billed to **issuer audit clients** and were attributable to each of (1) audit services, (2) other accounting services, (3) tax services, and (4) non-audit services; even though the reporting period ends on March 31 of each year, Form 2 allows the firm to report these percentages on the basis of the fees earned during the fiscal year ending immediately prior to the information cut-off date of March 31
- for each issuer for which the firm issued an audit report during the period, the issuer's name, the issuer's CIK number and the date of the audit report
- the range of the total number of firm personnel who had the authority to sign an audit report during the reporting period
- if the firm did not issue an audit report but played a significant role in the preparation or furnishing of an audit report, the firm must disclose the name and CIK number of each issuer, the registered firm that issued the audit report, the end date of the fiscal period covered by the audit report, and a description of the substantial role played by the firm
- the firm must describe any membership or affiliation

with any network, alliance, arrangement, partnership or association that licenses or authorizes audit procedures, audit manuals, the use of a name in connection with the provision of audit services, and any arrangement by contract or otherwise with another entity through which the firm employs or leases personnel to perform audit services (i.e., an alternative practice structure)

- the firm must describe whether as of March 31, the firm has any employee, partner, shareholder, principal, member or owner, or has acquired any entity or has an agreement to secure consulting services from an entity who was the subject of a disciplinary sanction by the PCAOB or a Commission order entered within the preceding five years, and who provides audit services to the firm's audit clients
- the firm must disclose whether it has acquired another public accounting firm during the reporting period

In addition, Form 2 also requires an annual affirmation that the firm consents to cooperate with the PCAOB and enforce cooperation with the PCAOB by the firm's associated persons. The firm's affirmation is strictly required, subject only to exceptions imposed by non-US legal requirements.

In order to be accepted for filing, the Form 2 must also include a signed certification by an authorized partner or officer of the firm. Such certification confirms completeness of the Form 2 and also confirms that the firm has filed all required Special Reports on Form 3 during the applicable reporting period. If the firm realizes that it has not filed a required Form 3, it must complete and file such Special Report before it can file the Form 2 with the required certification. If the PCAOB discovers that the Form 2 Annual Report is untrue, incomplete or misleading, the PCAOB can take disciplinary action against the firm for violating the reporting requirements, and potentially against any associated person who caused the firm's violation.

The PCAOB adopted a single filing deadline rather than allowing registered public accounting firms to file based on their respective fiscal years. Rule 2201 sets June 30 of each year as the deadline for the annual filing of Form 2. The reporting period covered by the annual report is April 1 to March 31, leaving each firm with three months to prepare and file a Form 2 reflecting information from that 12-month period. Any firm that was registered as of March 31 of a particular year would be required to file Form 2 by June 30 of that

year, but any firm that became registered in the period between and including April 1 and June 30 would not be required to file a Form 2 until June 30 of the following year. Each currently registered firm's first Form 2 Annual Report is due June 30, 2009.

### *Special Report*

The PCAOB adopted Form 3 which requires a registered accounting firm to report certain material events that are not reflected in the firm's information on file with the PCAOB. Its principal purpose is to alert the PCAOB about events that may have more immediate bearing on how the PCAOB carries out its regulatory responsibilities regarding the firm. These reportable events include a change in the firm's name or contact information, the institution of certain types of legal, administrative, or disciplinary proceedings against a firm or certain categories of individuals and the taking on of individuals or entities meeting certain criteria regarding disciplinary history. Also, a reportable event includes entering into an arrangement to receive from individuals or entities with certain disciplinary history, services related to the firm's audit practices or services the firm provides to issuer audit clients.

Rule 2203 requires a firm to file a Special Report no later than 30 days after the triggering event. Triggering events are described in Form 3 as having occurred when the firm has "become aware" that such triggering event has occurred. **The firm is deemed to become aware when any partner, shareholder, principal, owner or member of the firm first becomes aware of the facts underlying such event.** Also, firms may file amendments to those Special Reports if the original Special Report contains incorrect information. When filing a Form 3 to amend an earlier Special Report, the firm must supply not only the amended and supplemental information, but must include all information, affirmations, and certifications that were required to be included in the original Form 3. The PCAOB anticipates that reportable events will not routinely occur and that firms will go through most years without having any reportable events.

In addition to requiring firms to file Special Reports going forward, Rule 2203 includes requirements designed to eliminate information and reporting gaps that may be caused by two events. First, certain information on a firm's Form 1 initial application for registration need not have been any more current than as of the

date 90 days before the application is submitted. For firms that become registered after that date, Rule 2203 addresses the gap by requiring that within 30 days of becoming registered, the firm must file a Form 3 concerning any reportable events that occurred between the firm's Form 1 information cut-off date and the date of registration. A second possible cause is the passage of time that has occurred since the Form 1 information cut-off date used by firms that have been registered since 2003 or 2004.

### *Initial Special Report*

Of immediate significance to firms already registered, Rule 2203(a)(3) requires such firms to file a "bring current" Special Report on Form 3 to the extent that certain events have occurred since the date of the information contained in its original Form 1 registration and only to the extent that information about those events has current relevance.

**This initial Special Report is due within 30 days after the effectiveness of Rule 2203 (which will mean a total of 90 days after approval by the SEC).**

The events required to be reported in the initial Special Report are as follows:

**Criminal Proceedings**

- Pending criminal proceedings or the conclusion of any criminal proceedings against the firm or any of the firm's partners, shareholders, principal, owners, members or audit managers ("Key Persons")
- A Key Person who provided at least 10 hours of audit services for any issuer during the current fiscal year or the most recently completed fiscal year has become a defendant in a criminal proceeding and is charged with fraud, embezzlement, forgery, extortion, bribery, obstruction of justice, perjury or false statements, or is charged with any crime arising out of alleged conduct relating to accounting, auditing, securities, banking, commodities, taxation, consumer protection or insurance, or any such proceeding has been concluded

**Civil Proceedings**

- In a matter arising out of the provision of professional services for an issuer, the firm, a Key Person who has provided services for such issuer, or a Key Person who has provided at least 10 hours of audit services for any issuer during the firm's current fiscal year or the most recently completed fiscal year, has become a

defendant or respondent in a civil or alternative dispute resolution proceeding initiated by a governmental entity or in an administrative or disciplinary proceeding other than a PCAOB disciplinary proceeding

- The firm, or the parent or subsidiary of the firm, has become the subject of a bankruptcy petition or a receiver or trustee has been appointed to administer the assets or business of the firm or its parent or subsidiary

**Disciplinary Sanctions**

- The firm has hired as employee, partner, shareholder, principal or member, or has otherwise become owned or partly owned, by a person who is currently the subject of (i) an effective PCAOB disciplinary sanction suspending or barring the person from being an associated person of a registered firm, or (ii) an effective Commission order suspending or denying the privilege of appearing or practicing before the Commission
- The firm has become owned or partly owned by an entity that is currently the subject of (i) a PCAOB disciplinary sanction suspending or revoking the entity's registration, or (ii) an effective Commission order suspending or denying the privilege of appearing

or practicing before the Commission

- The firm has entered into a contractual or other arrangement to receive consulting or other professional services from a person or entity who is the subject of a PCAOB disciplinary sanction or Commission order of the type described above

**Audit Clients**

- The number of the firm's issuer audit clients has crossed one way or the other over the 100 issuer audit client threshold (which has an impact on the frequency of PCAOB inspections)
- The firm has withdrawn an audit report on financial statements and the issuer failed to comply with its reporting requirements on Form 8-K under the Securities Exchange Act of 1934

**Accounting Licenses**

- The firm's accounting license in a particular jurisdiction has ceased to be effective or has become subject to conditions or contingencies not applicable to all firms generally in such jurisdiction
- The firm has obtained an accounting license in a jurisdiction which has not been previously disclosed to the PCAOB, or if there has

been a change in the license number previously identified in a PCAOB filing

### ***Name and Address Changes***

- The firm has changed its legal name, though remaining the same legal entity, since the date of its original registration with the PCAOB
- The mailing address, telephone number, facsimile number or business e-mail or the firm's primary contact with the PCAOB has changed

### ***Public Availability of Reports***

Each firm's annual and special reports will be made available to the public on the PCAOB's website, subject to exceptions for information that satisfies specified criteria for confidential treatment. A firm may not request confidential treatment for specified types of information, including, for example, information about the firm's annual billings, the identity of the firm's issuer audit clients, the firm's affiliation with a network or alliance, or the identity of an issuer with respect to which the firm has withdrawn its audit report.

### ***Preparing for Reporting***

The new reporting rules will take effect 60 days after approval by the Commission. Registered accounting firms should be

cognizant of the applicable deadlines for the required reports:

- **Initial Special Report:** the first report due after the rules take effect will be the "bring current" Special Report on Form 3; within 30 days after the effectiveness of the rules, firms must file a Special Report if any of the circumstances enumerated above have occurred since the firm's initial registration with the PCAOB
- **Annual Report:** the first annual report on Form 2 will be due by June 30, 2009, for the 12-month period ending March 31, 2009
- **Special Report:** to the extent that any of the triggering events described above occur after the firm files its initial Special Report but prior to being reported on an Annual Report, the firm must file an additional Special Report describing such events.

In order to prepare the new reporting regimen, firms would be well served by starting the internal review process as soon as possible and by setting up internal reporting systems that will report triggering events to the management personnel in charge of regulatory compliance for the firm. A firm's first task should be to review its initial PCAOB registration filing, which may be several years old. That filing should be compared to the

requirements of the new Form 3 to determine whether an initial Special Report will be required once the new rules become effective. A firm should also modify its internal regulatory compliance checklists and questionnaires in order to collect systematically the type and extent of information required by both the Form 2 Annual Report and the Form 3 Special Report. Finally, the firm should be educating its partners, members and professional staff as to the level of information that must be reported internally on a timely basis in order to assure that the firm remains in compliance with its reporting obligations with the PCAOB. The PCAOB's release adopting the rules, along with the text of the rules and the instructions to Form 2 and Form 3 can be found on its website, [www.pcaobus.org](http://www.pcaobus.org), on the Rulemaking Docket under Rules (Docket Matter No. 019).

If you have questions concerning the new PCAOB reporting requirements, please contact a member of Vedder Price's Accountants Professional Services Group. ■

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- organization and structuring of accounting firms, and the acquisition of accounting practices
- compliance with Sarbanes-Oxley and other securities laws requirements, PCAOB rules and regulations, state laws and regulations and professional codes of ethics

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