



The Bond Market Association  
360 Madison Avenue  
New York, NY 10017



**Securities Industry Association**

Securities Industry Association  
120 Broadway  
New York, NY 10271

October 13, 2005

Mr. Donald T. Nicolaisen,  
Chief Accountant  
Mr. Alan L. Beller, Director,  
Director, Division of Corporation Finance  
Ms. Carol Stacey,  
Chief Accountant, Division of Corporation Finance  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549

Re: Positions taken by the AICPA at Oct. 11 meeting  
confirm that White Paper II must be publicly repudiated

Ladies and Gentlemen:

The Bond Market Association and the Securities Industry Association are writing to report to you, as you had requested, about the October 11, 2005 meeting hosted by the AICPA that we attended concerning their proposal (White Paper II) effectively to withdraw from the due diligence process in securities offerings, to the detriment of investors.

This letter describes:

- counterproductive positions taken by the AICPA at the meeting, which indicate that despite our letter of last week they do not yet accept that, in the interest of investor protection, full auditor participation in due diligence discussions is critical,
- our request that the AICPA publicly repudiate White Paper II and instruct auditors that White Paper II may not be referred to or implemented in any manner, and that the SEC and PCAOB encourage them to do so, and
- our view that the only way forward, if the AICPA wishes guidance in this area, is a process that includes investors and regulators, and not further private meetings as requested by the AICPA.<sup>1</sup>

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<sup>1</sup> The Bond Market Association is an international trade association representing approximately 200 securities firms and banks that underwrite, distribute and trade in fixed income securities in the

**ANTI-INVESTOR POSITIONS TAKEN BY AICPA**

We were dismayed by the remarks made by the representatives of the Big Four audit firms who spoke as members of the AICPA task force. Despite having received our letter last week that clearly expressed our concerns that White Paper II would withdraw auditors from a vital investor protection function and jeopardize the quality of financial disclosure, and despite reports of SEC staff concerns, the AICPA continued to press the themes espoused in White Paper II. The following statements made at the meeting are of greatest concern:

- ***Auditing standards for written reports govern oral discussions.*** The AICPA continued to assert that existing auditing standards governing attestation reports and other formal written reports also apply to oral due diligence discussions.
  - This is just wrong, as evidenced by decades of auditor involvement in due diligence without reference to auditing standards as a limitation on what may be discussed.
  - Furthermore, only the PCAOB is authorized to interpret the applicability of existing standards to matters for which they were not originally intended, such as oral due diligence discussions.
- ***Auditor participation in due diligence should be narrowed.*** The AICPA continued to push the idea that the auditors and underwriters should work privately to agree on *limitations* on the auditors' role.
  - Instead, we believe that the level of auditor involvement in due diligence should be enhanced and, at a minimum, restored to the level that prevailed in years past.
- ***Investors and regulators should continue to be excluded.*** The AICPA repeatedly urged that private negotiations should continue between auditors and underwriters with a view to limiting auditor participation in due diligence, while deferring investor and regulator input. Proceeding without the involvement of key constituencies is no way forward.

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U.S. and internationally. More information about the TBMA and its members and activities is available on its website [www.bondmarkets.com](http://www.bondmarkets.com).

The Securities Industry Association brings together the shared interests of nearly 600 securities firms to accomplish common goals. SIA members, including investment banks, broker-dealers and mutual fund companies, are active in U.S. and foreign markets and in all phases of corporate and public finance. More information about the SIA and its members and activities is available on its website [www.sia.com](http://www.sia.com).

- ***No rationale for this important change is needed.*** Despite repeated requests by various meeting participants, no understandable rationale was offered by the AICPA for their desire to reduce auditor due diligence involvement.
- We were told that guidelines were needed to bring “consistency” to responses by audit partners to due diligence inquiries that are perceived as off-limits. This is not a rationale, but instead an expression of the AICPA’s desired end result – that there be a “standard” that can be used to press audit partners who are still engaging in open due diligence discussions to consistently limit their involvement in due diligence. We still do not know why that is appropriate or furthers investor protection. No examples were given to suggest that new guidelines would *increase* auditor involvement in due diligence, as opposed to permitting or requiring them to drop to even more reduced levels of involvement.
- To the extent a guideline is needed at all, we suggest the following, which was the widely understood principle that successfully governed auditor involvement in due diligence for decades: “Auditors who are asked by their audit clients to participate in due diligence should speak freely during due diligence about matters of which they have knowledge and which are within their professional competence; limitations of auditing standards covering formal written reports do not apply to oral due diligence.” Over the past few years, we have observed a disturbing trend of auditor withdrawal from the due diligence process, which culminated in White Paper II.
- We were also told that because there is less time for due diligence in fast shelf takedowns, auditors are somehow justified in withdrawing more. This is illogical and contrary to investor protection principles that have been reflected in recent court decisions, such as WorldCom.

These statements of the AICPA illustrate to us that the AICPA is not yet prepared to return to the collaborative approach to due diligence in crafting good disclosure that had prevailed for decades.

#### **OUR MAIN REQUESTS TO AICPA**

Consistent with the views expressed in our letter last week, we made three main requests to the AICPA at the meeting:

- ***Publicly repudiate White Paper II.*** First, the AICPA should publicly repudiate White Paper II. If that were done effectively, and the *status quo* of free auditor participation in due diligence were restored to the level that prevailed in years past, we believe no further action would be required.
- ***Do not issue further versions of White Paper II.*** Second, it would not be helpful for the AICPA to issue a “new and improved” version of White Paper II. For

example, it would be unacceptable if the AICPA were to create a new draft that omits the most egregious positions of White Paper II but that still narrows auditor participation in due diligence. Regulators and not auditors should be drafting any guidance in this area. That guidance should encourage *increased* auditor participation in due diligence. White Paper II cannot be fixed.

- ***Establish a fair forum that includes investors, regulators and other interested parties.*** Third, if the AICPA wishes to pursue the subject, establish an inclusive and fair forum that
  - includes investors, directors, issuers and other interested parties from the outset,
  - has investor protection as its overall goal (which means expanding, not narrowing, the auditors' role in due diligence), and
  - is conducted under the oversight or with the participation of the SEC and PCAOB.

We believe a process that involves the regulators is required, rather than private negotiations, because the AICPA continues to insist that auditing standards for written attestations also govern oral due diligence discussions and continues to urge that the auditors' role in due diligence be narrowed rather than expanded.

As noted above, we asked the AICPA, as a necessary first step, to publicly repudiate White Paper II (not merely withdraw it). Repudiation means making a public statement that White Paper II does not correctly describe the relationship of auditing standards to oral due diligence discussions and that the auditors' involvement in due diligence is not limited by auditing standards. The AICPA reaction to that request at the meeting was they could not do so because they disagreed with it. Without such a public statement, we believe the ideas in White Paper II will infect auditors' attitudes towards the due diligence process and that auditors' participation will continue to diminish. That would be contrary to the public policy of the federal securities laws.

## **MEETING PARTICIPANTS**

As background, the meeting lasted two hours and was attended for the AICPA by representatives of six audit firms.<sup>2</sup> It was attended for us by representatives of nine investment banks,<sup>3</sup> having received input from numerous other firms that are members of our Associations, as well as senior staff of our Associations. Also in

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<sup>2</sup> BDO Seidman, Deloitte & Touche, Ernst & Young, Grant Thornton, KPMG and PricewaterhouseCoopers.

<sup>3</sup> Banc of America Securities, Citigroup Global Markets, Credit Suisse First Boston, Goldman, Sachs, JP Morgan Chase, Lehman Brothers, Merrill Lynch, Morgan Stanley and UBS Securities.

attendance at the invitation of the AICPA were representatives of the New York City Bar Association's Financial Reporting Committee and of several law firms.

## CONCLUSION

We respectfully request that the SEC encourage the AICPA to publicly repudiate White Paper II, as described above, by issuing a public statement that White Paper II does not correctly describe the relationship of auditing standards to oral due diligence discussions and that the auditors' involvement in due diligence is not limited by auditing standards.

In addition to the persons noted below, we are sending copies of this letter to the investor, director and issuer organizations to which last week we sent our letter describing our concerns with the AICPA's White Paper II initiative. We urge these organizations to express their concerns directly to the SEC and the PCAOB about the anti-investor direction of White Paper II and about having been excluded by the AICPA from the process.

If you wish to contact the Associations about this letter, please do so through Sarah Starkweather, Regulatory Counsel at The Bond Market Association (tel: 646-637-9292; e-mail: sstarkweather@bondmarkets.com) or Eileen Ryan, Associate General Counsel, at the Securities Industry Association (tel: 212-618-0508; e-mail: eryl@sia.com), who will coordinate with the appropriate members and staff of both Associations.

Very truly yours,

Micah S. Green,  
President and CEO  
The Bond Market Association

Marc E. Lackritz,  
President  
Securities Industry Association

cc:

Hon. William J. McDonough, Chairman  
Hon. Kayla J. Gillan, Member  
Hon. Daniel L. Goelzer, Member  
Hon. Bill Gradison, Member  
Hon. Charles D. Niemeier, Member  
Dr. Douglas R. Carmichael, Chief Auditor and Director of Professional Standards  
Members of Standing Advisory Group  
(Public Company Accounting Oversight Board)

Hon. Christopher Cox, Chairman  
Hon. Paul S. Atkins, Commissioner  
Hon. Roel C. Campos, Commissioner  
Hon. Cynthia A. Glassman, Commissioner  
Hon. Annette L. Nazareth, Commissioner  
(Securities and Exchange Commission)

Center for Public Company Audit Firms  
(American Institute of Certified Public Accountants)