

the information to monitor principal trades in their accounts.

The Commission staff estimates that approximately 380 investment advisers make use of rule 206(3)-3T, including an estimated 24 advisers (on an annual basis) also registered as broker-dealers who do not offer non-discretionary services, but whom the Commission staff estimates will choose to do so and rely on rule 206(3)-3T. The Commission staff estimates that these advisers spend, in the aggregate, approximately 378,992 hours annually in complying with the requirements of the rule, including both initial and annual burdens. The aggregate hour burden, expressed on a per-eligible-adviser basis, is therefore approximately 997 hours per eligible adviser (378,992 hours divided by the estimated 380 advisers that will rely on rule 206(3)-3T).

Written comments are invited on:

(a) Whether the collections of information are necessary for the proper performance of the functions of the Commission, including whether the information has practical utility; (b) the accuracy of the Commission's estimate of the burdens of the collections of information; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burdens of the collections of information on respondents, including through the use of automated collection techniques or other forms of information technology. Consideration will be given to comments and suggestions submitted in writing within 60 days of this publication.

Please direct your written comments to Thomas Bayer, Director/CIO, Securities and Exchange Commission, C/O Remi Pavlik-Simon, 6432 General Green Way, Alexandria, VA 22312; or send an e-mail to: PRA_Mailbox@sec.gov.

Dated: December 27, 2010.

Florence E. Harmon,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-63606; File No. PCAOB 2010-01]

Public Company Accounting Oversight Board; Order Approving Proposed Rules on Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Related Amendments to PCAOB Standards

December 23, 2010.

I. Introduction

On September 15, 2010, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission") a notice (the "Notice") of proposed rules (File No. PCAOB 2010-01) on Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Related Amendments to PCAOB Standards. Those eight auditing standards (hereinafter referred to as "Risk Assessment Standards"), which will supersede six of the Board's interim auditing standards, are:

- Auditing Standard ("AS") No. 8, *Audit Risk*;
- AS No. 9, *Audit Planning*;
- AS No. 10, *Supervision of the Audit Engagement*;
- AS No. 11, *Consideration of Materiality in Planning and Performing an Audit*;
- AS No. 12, *Identifying and Assessing Risks of Material Misstatement*;
- AS No. 13, *The Auditor's Responses to the Risks of Material Misstatement*;
- AS No. 14, *Evaluating Audit Results*; and
- AS No. 15, *Audit Evidence*.

Notice of the proposed rules was published in the **Federal Register** on September 27, 2010.¹ The Commission received two comment letters relating to the proposed rules. For the reasons discussed below, the Commission is granting approval of the proposed rules. As specified by the Board, the rules are effective for audits of fiscal years beginning on or after December 15, 2010.

II. Description

The Board adopted eight auditing standards and related amendments that are designed to benefit investors by establishing requirements that enhance the effectiveness of the auditor's

assessment of and response to the risks of material misstatement in an audit. Assessing and responding to risks underlies the entire audit process. The risk assessment standards that the PCAOB is replacing were part of the Board's interim standards and were in large part written twenty to thirty years ago. In adopting the new Risk Assessment Standards, the Board intended to build upon and improve the risk framework that was already established by the interim standards, rather than replacing that framework altogether.

Changes that the Board made to the interim standards reflect: Improvements that the PCAOB has observed in the audit methodologies of many registered firms; recommendations from academia; recommendations from the Board's Standing Advisory Group ("SAG") and other groups; the adoption of AS No. 5, *An Audit of Internal Control Over Financial Reporting That is Integrated with an Audit of Financial Statements*; improvements made to similar risk assessment standards by other standard setters (e.g., the International Auditing and Assurance Standards Board ("IAASB") and the Auditing Standards Board ("ASB") of the American Institute of Certified Public Accountants); and observations from the Board's oversight activities.

Key changes made to the standards include an increased emphasis on fraud risks, an increased emphasis on disclosures, inclusion of multi-location audit requirements, an alignment of the standards with AS No. 5, and inclusion of a concept of materiality more specifically grounded to that used in the Federal securities laws.

III. Discussion

The Commission received two comment letters: One from Deloitte & Touche, LLP ("Deloitte") and one from the Center for Capital Markets Competitiveness of the U.S. Chamber of Commerce ("CMCC"). Deloitte supported approval of the standards, while expressing certain concerns largely of a more general nature regarding the PCAOB's approach to standard-setting. The CMCC believed that the Risk Assessment Standards should not be approved, but rather sent back to the PCAOB in order for the PCAOB to address certain concerns, most of which also related to the PCAOB's overall approach to standard-setting as opposed to the particular standards at issue.

¹ See Release No. 34-62919 (September 15, 2010) [75 FR 59332 (September 27, 2010)]. The notice included a 21-day comment period. The comment period closed on October 18, 2010.

Integration of Fraud Risk Standard Into the Risk Assessment Standards

One of the significant changes to the Risk Assessment Standards was the incorporation of aspects of AU sec. 316, *Consideration of Fraud in a Financial Statement Audit*, into the Risk Assessment Standards. In explaining why the PCAOB incorporated portions of the fraud standard into the Risk Assessment Standards, it stated that:

Incorporating these requirements makes clear that the auditor's responsibilities for assessing and responding to fraud risks are an integral part of the audit process rather than a separate, parallel process. It also benefits investors by prompting auditors to make a more thoughtful and thorough assessment of fraud risks and to develop appropriate audit responses.²

The CCMC did not agree with the level of integration. The CCMC made a similar comment during the PCAOB's due process stage, which the Board addressed in its adopting release. This comment largely relates to a disagreement as to the manner in which the standards are constructed, as compared to the performance required of auditors. The Commission believes that the PCAOB has given due consideration to the comments received about this matter.

Effective Date

The effective date of the standards will be for audits of fiscal years beginning on or after December 15, 2010. The CCMC expressed concern about the effective date, stating that the effective date "would not allow adequate time for audit firms to revise their audit methodologies and train their audit staffs around the world for audits in 2011." In response to similar concerns raised in its comment letter process, including from the CCMC, the PCAOB stated in its release that the underlying concepts of risk-based auditing have not changed, and therefore, while there are many incremental requirements in the updated standards, these standards should not require wholesale changes to audit methodologies.³ Any delay in the effective date of these standards would likely delay the implementation for most issuers for at least one year (*e.g.*, the standards would not be applicable generally until calendar year 2012 audits related to audit reports to be issued in 2013).

After considering the nature of the changes in the Risk Assessment

Standards, the timing of Commission approval, and the fact that the standards will not be applicable to audits for which audit reports will be issued in 2011 (*i.e.*, the first audit reports issued for which audits would be required to be conducted using the new standards would not be issued until 2012) we believe the PCAOB's approach for implementation is not unreasonable.

PCAOB Standard-Setting Process

Both commenters noted various concerns about the PCAOB's standard-setting process. The concerns identified included divergence from other standard-setters, what the commenters viewed as a "prescriptive" nature of the standards, the lack of a codification of PCAOB standards, the usefulness of the appendix that compares the PCAOB proposed standard to the similar standards of other standard-setters, and the use of certain terms in the standards. These comments all relate more to the PCAOB's overall approach to standard-setting than particular concerns with respect to the individual Risk Assessment Standards.

All of these comments are similar to those received by the PCAOB during its standard-setting process, which the Board addressed. For example with respect to divergence from other standard-setters, the Board noted the following:

In previous releases on its proposed risk assessment standards, the Board has stated that it has sought to eliminate unnecessary differences with the risk assessment standards and those of other standards-setters. However, because the Board's standards must be consistent with the Board's statutory mandate, differences will continue to exist between the Board's standards and the standards of the IAASB and ASB, *e.g.*, when the Board decides to retain an existing requirement in PCAOB standards that is not included in IAASB or ASB standards. Also, certain differences are often necessary for the Board's standards to be consistent with relevant provisions of the federal securities laws or other existing standards or rules of the Board.⁴

The Board also noted that it "continually endeavors to improve its processes" and explained other initiatives it uses in both gaining input on its standard-setting activities (*e.g.*, through its SAG and by releasing multiple exposure documents) and providing additional transparency of its standards-setting process (*e.g.*, through posting its standards-setting agenda and enhanced discussions in its releases on the Board's conclusions). The

Commission notes and encourages the Board's efforts to consider standards issued by the IAASB and the ASB, and appreciates the reasons why it is reasonable to expect that the Board's standards may appropriately differ from such standards. The Commission and its staff will continue to provide oversight of the Board and its staff's ongoing endeavor to improve its processes.

Regarding the "prescriptive" nature of the standards, we recognize that there should be an appropriate balance in auditing standards between providing necessary minimum requirements and allowing auditors to apply judgment in determining the nature and extent of audit procedures given the particular circumstances of an individual engagement. PCAOB standards recognize that the auditor uses judgment in planning and performing audit procedures and evaluating the evidence obtained from those procedures. We recognize, however, that overly broad standards without an appropriate balance of necessary requirements could lead to a level of discretion in the nature and extent of audit procedures that may limit the effectiveness of audits. The Commission believes the PCAOB's approach in the Risk Assessment Standards is not unreasonable and encourages the PCAOB to monitor implementation and evaluate the input received during the development of future standards to continue to strive to achieve an optimal balance.

Regarding a codification of the auditing standards, the Commission notes that the Board has recently added this project to its strategic plan and amended its performance measure on standard-setting activities to reflect this new initiative.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed PCAOB Rules on Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Related Amendments to PCAOB Standards (File No. PCAOB-2010-01) are consistent with the requirements of the Sarbanes-Oxley Act of 2002, as amended (the "Act") and the securities laws and are necessary or appropriate in the public interest or for the protection of investors.

It is therefore ordered, pursuant to Section 107 of the Act and Section 19(b)(2) of the Securities Exchange Act of 1934, that the proposed PCAOB Rules on Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Related Amendments to PCAOB Standards (File No. PCAOB-2010-01) be and hereby are approved.

² PCAOB Release No. 2010-004, August 5, 2010, p. 3.

³ PCAOB Release No. 2010-004, August 5, 2010, p. 8.

⁴ See PCAOB Release No. 2010-004, August 5, 2010, pp. A10-91—A10-92 (internal footnotes omitted).

By the Commission.

Elizabeth M. Murphy,
Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-63603; File No. SR-Phlx-2010-180]

Self-Regulatory Organizations; NASDAQ OMX PHLX LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Revising Floor Qualification Examination

December 22, 2010

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4² thereunder, notice is hereby given that on December 10, 2010, NASDAQ OMX PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change, and an amendment thereto on December 15, 2010, as described in Items I, II, and III, below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.³

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to revise its floor qualification examination. Specifically, the Exchange proposes to delete obsolete questions, revise outdated questions and add several new questions, as described further below.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of the proposed rule change is to improve the Exchange’s program for qualification of members by updating its floor qualification examination. The Exchange has employed a written floor qualification examination, which is required for persons seeking to act as members on the trading floor,⁴ for many years. The examination, which has not been substantively amended for many years,⁵ covers many areas of the Exchange’s rules.

At this time, the Exchange proposes to update the exam in a variety of ways. The exam would continue to be comprised of 100 questions, randomly and electronically selected from a question bank of approximately 148 questions. The floor qualification examination is administered by the Exchange’s membership department, and requires a passing score of 70 during a 75 minute testing period.

In terms of outdated questions, the Exchange proposes to delete about 31 obsolete questions, mostly pertaining to: (i) The “Wheel,” an obsolete method of allocating trades among specialist and Registered Options Traders (“ROTs”); (ii) “AUTO-X” functionality and specialists manually conducting an opening and executing trades, which have been replaced by the current trading system, Phlx XL II; and (iii) the “ten-up” guarantees that preceded displayed size for options and the application of the Quote Rule to options.⁶

The Exchange also proposes to eliminate the foreign currency options qualification examination, because there have been no foreign currency options participants for many years.⁷ In addition, the Exchange no longer offers the foreign currency options products that were the subject of this examination, but rather now offers a U.S. dollar-settled foreign currency option,⁸ which trades pursuant to the

Exchange’s options trading rules that are covered on the floor qualification exam.

The Exchange proposes to modify approximately 17 questions pertaining to electronic quoting, various changes in priority rules and to reflect the existence of Options Exchange Officials (“OEOs”), who replaced Floor Officials, as well as make various minor corrections reflecting rule changes over time. Similarly, the Exchange proposes to add approximately 46 new questions reflecting trade reporting, disputes and OEO rulings, priority and trade allocation, spreads, openings, halts and reopening, quoting obligations, order types, Floor Broker obligations and Rule 703.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act⁹ in general, and furthers the objectives of Section 6(b)(5) of the Act¹⁰ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest. In addition, the Exchange believes that the proposed rule change is consistent with Section 6(c)(3)(B) of the Act,¹¹ which authorizes exchanges to prescribe standards of training, experience and competence for persons associated with exchange members, and gives exchanges the authority to bar a natural person from becoming a member or a person associated with a member, if the person does not meet the standards of training, experience and competence prescribed in the rules of the exchange. The Exchange believes that revising its floor member qualification examination should better test the knowledge of its floor members, and thereby enhance the Exchange’s standards for training, experience and competence.

B. Self-Regulatory Organization’s Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

⁴ See Rules 620(a) and 901(c). See also Rule 1061 applicable to Floor Brokers.

⁵ Securities Exchange Act Release No. 33304 (December 9, 1993), 58 FR 65613 (December 15, 1993)(SR-Phlx-92-34).

⁶ For current requirements, see e.g., Rules 1080 and 1082.

⁷ The Exchange intends to separately delete “foreign currency options participant” and related terms from its rules.

⁸ See Securities Exchange Act Release No. 54989 (December 21, 2006), 71 FR 78506 (December 29, 2006)(SR-Phlx-2006-34).

⁹ 15 U.S.C. 78f(b).

¹⁰ 15 U.S.C. 78f(b)(5).

¹¹ 15 U.S.C. 78f(c)(3)(B).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Amendment No. 1.