

generally would limit application of the rule to issuers whose securities are registered with the Commission under section 12 of the Exchange Act, that are required to file reports with the Commission under section 15(d) of the Exchange Act, or that have filed registration statements with the Commission that have not yet become effective and have not been withdrawn.⁹ We continue to believe that the definition of the term “issuer” in section 3 of the Exchange Act applies to the use of the term in the new rules.¹⁰ The term “issuer,” as defined in the Exchange Act, has been used in Rule 13b2-2 since it was adopted in 1979,¹¹ and we believe that the amendments do not require a change in the meaning of the term. In addition, because the new rule specifically applies to improperly influencing auditors of issuers’ financial statements “that are required to be filed with the Commission,” the commenter’s concern that this definition would extend the scope of the rule to all private issuers of securities has been addressed. Accordingly, the term “issuer” in the new rule should be defined as stated in section 3 of the Exchange Act.

Definition of “officer.” New rule 13b2-2(b)(1) addresses activities by an officer or director of an issuer, or any other person acting under the direction of an officer or director.¹² The Commission has defined the term “officer” to include the company’s “president, vice president, secretary, treasurer or principal financial officer, comptroller or principal accounting officer, and any person routinely performing corresponding functions

with respect to any organization whether incorporated or unincorporated.”¹³ The term “executive officer” includes an issuer’s chief executive officer and other officers who perform policy-making functions for the issuer.¹⁴

Some commenters suggested that the term “officer” should include all those responsible for corporate governance matters¹⁵ or who influence the preparation of an issuer’s financial statements.¹⁶ Commenters also suggested that the definition include an issuer’s general counsel or chief legal officer.¹⁷ We do not believe at this time that it is necessary to amend the existing definition of “officer” or “executive officer,” or to write a new definition specifically for Regulation 13B-2. The existing definitions cover, among others, those who set corporate governance policies and legal policies for an issuer. Should we note that members of management not encompassed by the existing definitions of “officer” and “executive officer” are engaging in the conduct addressed in the rule, we may revisit this issue.

Definition of “under the direction.” As noted above, new rule 13b2-2(b)(1) covers the activities of not only officers and directors of the issuer who engage in an attempt to misstate financial statements but also “any other person acting under the direction thereof.” Activities by such “other persons” currently may constitute violations of

the anti-fraud or other provisions of the securities laws¹⁸ or aiding or abetting¹⁹ or causing²⁰ an issuer’s violations of the securities laws. Section 303(a) and the new rule provide the Commission²¹ with an additional means of addressing efforts by persons acting under the direction of an officer or director to improperly influence the audit process and the accuracy of the issuer’s financial statements.

As noted in the proposing release, we interpret Congress’ use of the term “direction” to encompass a broader category of behavior than “supervision.”²² In other words, someone may be “acting under the direction” of an officer or director even if they are not under the supervision or control of that officer or director. Such persons might include not only the issuer’s employees but also, for example, customers, vendors or creditors who, under the direction of an officer or director, provide false or misleading confirmations or other false or misleading information to auditors, or who enter into “side agreements” that enable the issuer to mislead the auditor.²³ In appropriate circumstances, persons acting under the direction of officers and directors also may include not only lower level employees of the issuer²⁴ but also other partners or employees of the accounting firm (such as consultants or forensic accounting

¹⁸ See, e.g., Section 10(b) of the Exchange Act, 15 U.S.C. 78j, and Rule 10b-5 thereunder, 17 CFR 240.10b-5.

¹⁹ See, e.g., section 20(e) of the Exchange Act, 15 U.S.C. 78t(e).

²⁰ See, e.g., section 21C of the Exchange Act, 15 U.S.C. 78u-3.

²¹ Section 303(b) of the Act states, “The Commission shall have exclusive authority to enforce this section and any rule or regulation issued under this section.”

²² See, e.g., Webster’s Dictionary (9th edition), which defines “direction” to include not only guidance or supervision of action or conduct but also explicit instruction.

²³ See, e.g., *In the Matter of Ronald G. Davies*, Accounting and Auditing Enforcement Release No. (“AAER”) 1281 (June 29, 2000), which states, in part,

In early 1998, Davies learned information that should have alerted him to the fact that Hybrid’s sales personnel had concealed the existence of the side letter from the Company’s management and auditors. When Hybrid and its auditors, as part of the preparation of the Company’s financial statements, sought confirmation that Ikon had received no right of return, Davies provided a misleading audit response to the Company. * * * Davies actions described above allowed Hybrid personnel to circumvent internal controls and make false statements to the Company’s auditors, and caused Hybrid to make material misrepresentations and file inaccurate reports with the Commission. * * * Based on the foregoing, Davies caused violations of Sections 10(b), 13(a), 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-13, 13b2-1, and 13b2-2 thereunder.

²⁴ See, e.g., *In the Matter of John K. Bradley*, AAER 1568 (June 5, 2002).

⁹ Section 2(a)(7) of the Act, which states:

The term “issuer” means an issuer (as defined in section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c)), the securities of which are registered under section 12 of that Act (15 U.S.C. 78l), or that is required to file reports under section 15(d) (15 U.S.C. 78d(d)), or that files or has filed a registration statement that has not yet become effective under the Securities Act of 1933 (15 U.S.C. 77a *et seq.*), and that it has not withdrawn.

¹⁰ The Commission has broad rulemaking authority to prescribe illegal acts that contribute to the falsification of financial statements or the issuance of false or misleading audit reports. See, e.g., sections 10, 10A and 23(a) of the Exchange Act, 15 U.S.C. 78j, 78j-1 and 78s(a). See also section 3(a) of the Sarbanes-Oxley Act of 2002, which states, “The Commission shall promulgate such rules and regulations, as may be necessary or appropriate in the public interest or for the protection of investors, and in furtherance of this Act.”

¹¹ Exchange Act Release No. 15570 (February 15, 1979) [44 FR 10970].

¹² The rule applies to foreign private issuers as well as domestic issuers. In applying the rule to foreign private issuers, the terms “officer” and “director” would indicate those performing equivalent functions under the local laws and corporate governance practices where the issuer is domiciled.

¹³ Rule 3b-2 under the Exchange Act, 17 CFR 240.3b-2. A person may be an “officer” for purposes of Rule 3b-2 regardless of the person’s title or the legal entity with which he or she is associated. For example, officers of wholly owned subsidiaries of public companies and promoters may be “officers” of public companies.

The definition of “director” under the Exchange Act has a similar functional and flexible nature. See section 3(a)(7) of the Exchange Act, 15 U.S.C. 78c(a)(7), which states, “The term ‘director’ means any director of a corporation or any person performing similar functions with respect to any organization, whether incorporated or unincorporated.”

¹⁴ Rule 3b-7 under the Exchange Act, 17 CFR 240.3b-7, states, “The term ‘executive officer,’ when used with reference to a registrant, means its president, vice president of the registrant in charge of a principal business unit, division or function (such as sales, administration, or finance), any other officer who performs a policy making function or any other person who performs similar policy making functions for the registrant. Executive officers of subsidiaries may be deemed executive officers of the registrant if they perform such policy making functions for the registrant.”

¹⁵ Letter from the National Association of State Boards of Accountancy (“NASBA”) dated November 25, 2002.

¹⁶ Letter from Transparency International—USA, dated November 8, 2002.

¹⁷ Letters from PricewaterhouseCoopers LLP (“PwC”) dated November 25, 2002 and Transparency International—USA, dated November 8, 2002.