

“*Fraudulently influence*.” New rules 13b2–2(b)(1) and (c)(2) address certain actions “to coerce, manipulate, mislead, or fraudulently influence” the auditor of the issuer’s financial statements. Much of the conduct addressed by the rules, particularly efforts to “manipulate or mislead” the auditor, generally would be subject to other provisions of the securities laws and the Commission’s regulations, including the existing rules in Regulation 13B–2.⁴⁰ The new rules, however, would provide an additional means to address conduct to coerce, manipulate, mislead, or fraudulently influence an auditor during his or her examination or review of the issuer’s financial statements, including conduct that did not succeed in affecting the audit or review.⁴¹

In the proposing release, we noted that in the rule the word “fraudulently” modifies influence but not coerce, manipulate or mislead. Several commenters suggested that the Commission should amend this interpretation and state that “fraudulently” modifies all four types of conduct.⁴² Some commenters indicated that intent to materially mislead the auditor should be required⁴³ and others stated any attempt to purposely skew the issuer’s disclosure should violate the rule.⁴⁴ One commenter noted that fraudulent intent should not be required for officers, directors or employees, but should be required for third parties such as vendors and customers.⁴⁵

We have decided not to amend our view that the word “fraudulently” modifies only “influence.” To emphasize this point, we have reordered the words to place “fraudulently influence” at the end of the list instead of at the beginning.⁴⁶ The new rule,

therefore, reads that no officer or director or person acting under his or her direction “shall directly or indirectly take any action to coerce, manipulate, mislead, or fraudulently influence” any accountant engaged in the performance of an audit or review of an issuer’s financial statements.

In the context of the new rule, the words “coerce” and “manipulate” imply compelling the auditor to act in a certain way through pressure, threats, trickery, intimidation or some other form of purposeful action,⁴⁷ and further modifiers are not necessary. Regarding the term “mislead,” pre-existing rule 13b2–2 for many years has prohibited officers and directors from directly or indirectly making or causing to be made materially misleading statements to auditors. Causing⁴⁸ misleading statements to be made to auditors has included, and will continue to include, an officer or director entering into an arrangement with a third party to send a misleading confirmation or to provide other misleading information or data to the auditor of the issuer’s financial statements.⁴⁹ The new rule does not alter this approach. As noted above, a primary purpose for enactment of the Sarbanes-Oxley Act is the restoration of investor confidence in the integrity of financial reports. Such a purpose would not be served by imposing what would amount to a new scienter requirement on the pre-existing provision prohibiting officers and directors from causing misleading statements or omissions to be made to auditors.

Types of Conduct. As stated in the proposing release, types of conduct that the Commission believes could constitute improper influence (if the person engaged in that conduct knows or should know that the conduct, if successful, could result in rendering the

issuer’s financial statements materially misleading) include, but are not limited to, directly or indirectly:

- Offering or paying bribes or other financial incentives, including offering future employment or contracts for non-audit services,
- Providing an auditor with an inaccurate or misleading legal analysis,
- Threatening to cancel or canceling existing non-audit or audit engagements if the auditor objects to the issuer’s accounting,
- Seeking to have a partner removed from the audit engagement because the partner objects to the issuer’s accounting,
- Blackmailing, and
- Making physical threats.

The facts and circumstances of each case would be relevant to determining whether the conduct would violate the new rule.

Commenters had varied reactions to the illustrative list of the types of conduct that could be covered by the rule. Some commenters suggested that providing inaccurate or misleading information to internal auditors, as well as to independent auditors, should be deemed a violation of the rule.⁵⁰ While we believe that an officer or director, or person acting under the direction of an officer or director, providing misleading information to an internal auditor would be relevant to the status of the issuer’s internal accounting controls or disclosure controls, it would not appear to be related to the purpose of section 303 of the Act and the new rule, which is to protect and enhance the independent audit function.⁵¹

Other commenters suggested that, due to other safeguards in the Act, we should delete from the illustrative list the actions of offering future employment with the issuer⁵² and threatening to cancel audit or non-audit contracts for services.⁵³ These commenters indicated that section 206 of the Act, which requires a one-year “cooling off” period from the time certain officers of the issuer last participated as a partner or employee of

⁴⁰ See, e.g., *In the Matter of Donald F. Marcus and In the Matter of Harry P. Adler*, AAER 1715 (February 10, 2003); *SEC v. John F. Mortell, et al.*, AAER 1569 (June 5, 2002); *In the Matter of Ronald G. Davies*, AAER 1281 (June 29, 2000); and *In the Matter of Terry R. Kuntz and Richard J. Scheer*, AAER 720 (September 26, 1995).

⁴¹ It is the act of coercing, manipulating, misleading, or fraudulently influencing the auditor, for the purpose of rendering misleading financial statements, that is unlawful. There is no requirement in section 303(a) of the Act that the purpose be achieved.

⁴² See, e.g., letters from Wells Fargo dated November 22, 2002, the American Bar Association dated December 13, 2002, Sidley Austin Brown & Wood dated December 20, 2002, BDO Seidman LLP dated November 25, 2002, and Dechert dated November 25, 2002.

⁴³ Letter from Dorsey & Whitney LLP dated November 25, 2002.

⁴⁴ Letter from Association for Investment Management and Research dated December 12, 2002.

⁴⁵ Letter from Ernst & Young dated November 25, 2002.

⁴⁶ See letter from Robert Waxman dated November 25, 2002.

⁴⁷ See letter from Dorsey & Whitney LLP dated November 25, 2002.

⁴⁸ *KPMG LLP v. Securities and Exchange Commission*, 289 F.3d 109, 126 (D.C. Cir. 2002), which states, “We affirm the Commission’s determination that negligence is an appropriate basis for violations underlying a Section 21C cease-and-desist order* * *.” See *In the Matter of KPMG Peat Marwick LLP*, AAER 1360 (January 19, 2001), which states, “We hold today that negligence is sufficient to establish ‘causing’ liability under Exchange Act section 21C(a), at least in cases in which a person is alleged to ‘cause’ a primary violation that does not require scienter. Therefore, if Peat Marwick acted at least negligently with respect to whether its conduct would contribute to PORTA’s violations, Peat Marwick is liable under Section 21C(a) as a cause of those violations.”

⁴⁹ See, e.g., *In the Matter of Donald F. Marcus and In the Matter of Harry P. Adler*, AAER 1715 (February 10, 2003); *SEC v. John F. Mortell, et al.*, AAER 1569 (June 5, 2002); *In the Matter of Ronald G. Davies*, AAER 1281 (June 29, 2000); and *In the Matter of Terry R. Kuntz and Richard J. Scheer*, AAER 720 (September 26, 1995).

⁵⁰ See, e.g., letters from HarborView LLC dated October 29, 2002 and Council of Institutional Investors dated November 22, 2002.

⁵¹ To the extent that the work of the internal auditor is used by the independent auditor in conducting an audit or review of the issuer’s financial statements, however, misleading or inaccurate information provided to the internal auditor may be deemed to be provided to the independent auditor.

⁵² See, e.g. letter from Deloitte & Touche dated November 27, 2002.

⁵³ See, e.g. letters from Deloitte & Touche dated November 27, 2002, European Commission dated November 25, 2002, and Ernst & Young dated November 25, 2002.