

the accounting firm in an audit of the issuer's financial statements to the commencement of the audit,⁵⁴ provides sufficient protection against offering employment as a means of improperly influencing the auditor. Similarly, commenters indicated that the provisions in sections 201 and 202 requiring audit committee pre-approval of audit and non-audit services should be an adequate safeguard against the use of such services to improperly influence auditors.⁵⁵ Sections 201, 202 and 206, as well as the remainder of Title II of the Act, are designed to enhance the independence of auditors. We believe, however, services and employment opportunities that would not impair an auditor's independence nonetheless could provide financial incentives used to improperly influence or otherwise deter auditors from performing an appropriate audit. Accordingly, such actions continue to be possible mechanisms, assuming the other criteria in the rule are met, for violating the new rule.

Some commenters suggested qualifying other examples in the list. For example, commenters indicated that canceling or threatening to cancel an audit or non-audit engagement should be within the purview of the rule only if the action was taken because the auditor objects to the issuer's accounting.⁵⁶ One commenter expressed this notion in terms of a clear *quid pro quo* linking the offering of a contract for non-audit services with the intent to fraudulently influence the audit.⁵⁷ We acknowledge that there may be many legitimate reasons to replace individuals on an audit or review engagement, or to award or cancel audit or non-audit services. Such actions alone do not violate the new rule. When such actions, however, become the consideration used by an officer or director, or person acting under the

direction of an officer or director, to improperly influence the auditor, and that person knew or should have known that the result of his or her conduct could be materially misleading financial statements, then the actions fall within the scope of the rule.

Still other commenters suggested adding to the list activities such as: knowingly providing to the auditor inadequate or misleading information that is key to the audit,⁵⁸ transferring managers or principals from the audit engagement,⁵⁹ and when predicated by an intent to defraud, verbal abuse, creating undue time pressure on the auditors, not providing information to auditors on a timely basis, and not being available to discuss matters with auditors on a timely basis.⁶⁰ In the appropriate circumstances and upon satisfaction of the criteria in the rule, each of these actions could result in improper influence on the auditor.

Finally, most commenters addressing the issue stated that the Commission should not place in the rule any examples of the types of conduct that might violate the rule,⁶¹ and we have not done so.

Definition of "independent public or certified public accountant." The new rule addresses the improper influence of "any independent public or certified public accountant" engaged in the performance of an audit or review of an issuer's financial statements.⁶² Prior to the adoption of the Act, similar phrases commonly were used in the securities laws and the Commission's regulations to refer to the accountant providing audit and review services to a Commission registrant. Although the Act, in anticipation of accounting firms registering with the Public Company Accounting Oversight Board (the "Board"),⁶³ changed several of these

references,⁶⁴ such terms continue to appear in certain sections of the securities laws⁶⁵ and related schedules.⁶⁶ We believe that section 303 of the Act includes all accountants⁶⁷ engaged in auditing or reviewing an issuer's financial statements or issuing attestation reports⁶⁸ to be filed with the Commission. Once firms are registered with the Board, the term "independent public or certified public accountant," as used in the new rule, would include registered public accounting firms⁶⁹ and persons associated with such a public accounting firm,⁷⁰ as defined in the Act. While some commenters expressed concern with the use of different definitions to describe the independent auditor,⁷¹ they generally

determines that the Board, as established by Title I of the Act, is appropriately organized and has the capacity to carry out and enforce the requirements of that title, it shall be unlawful for any person that is not a registered public accounting firm to prepare any audit report with respect to any issuer.

⁶⁴ See, e.g., sections 205(b) and (c) of the Act.

⁶⁵ See, e.g., section 13(a) of the Exchange Act, 15 U.S.C. 78m(a), and section 8(e) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. 77h(e).

⁶⁶ See, e.g., items 25, 26 and 27 of Schedule A of the 1933 Act, 15 U.S.C. 77aa(25), (26) and (27).

⁶⁷ The rule would apply regardless of whether the accountant was a certified public accountant. For example, some states require accountants to have years of experience before being deemed to be a CPA. Efforts to mislead such an individual during his or her performance of audit procedures would fall within the rules. In addition, the term "independent public or certified public accountant" includes accountants in foreign countries who engage in auditing or reviewing an issuer's financial statements or issuing attestation reports to be filed with the Commission, regardless of the title or designation used in those countries.

⁶⁸ See, e.g., section 404 of the Act, which mandates that the Commission prescribe rules that require (1) each annual report filed under sections 13(a) and 15(d) of the Exchange Act contain a management statement of responsibilities for, and assessment of the effectiveness of, the issuer's internal control structure and procedures for financial reporting, and (2) the auditor to attest to, and report on, the assessment made by management.

⁶⁹ Section 2(a)(12) of the Act defines "registered public accounting firm" to mean "a public accounting firm registered with the Board in accordance with this Act."

⁷⁰ Section 2(a)(9)(A) of the Act defines "person associated with a public accounting firm" (or with a "registered public accounting firm") to mean "any individual proprietor, partner, shareholder, principal, accountant, or other professional employee of a public accounting firm, or any other independent contractor or entity that, in connection with the preparation or issuance of any audit report—(i) shares in the profits of, or receives compensation in any other form from, that firm, or (ii) participates as agent or otherwise on behalf of such accounting firm in any activity of that firm." The Board, in section 2(a)(9)(B) of the Act, is given limited authority to exempt persons performing only ministerial tasks.

⁷¹ See, e.g., letters from Independent Community Bankers of America dated November 25, 2002 and Robert Waxman dated November 25, 2002.

⁵⁴ Section 206 of the Act adds section 10A(l) to the Exchange Act, which states:

It shall be unlawful for a registered public accounting firm to perform for an issuer any audit service required by this title, if a chief executive officer, controller, chief financial officer, chief accounting officer, or any person serving in an equivalent position for the issuer, was employed by that registered public accounting firm and participated in any capacity in the audit of that issuer during the 1-year period preceding the date of the initiation of the audit.

⁵⁵ Section 201 of the Act prohibits the auditor of the issuer's financial statements from providing certain non-audit services for that issuer and permits other non-audit services to be performed only if the service is pre-approved by the issuer's audit committee. Section 202 of the Act describes the pre-approval process.

⁵⁶ See, e.g., letter from America's Community Bankers dated November 25, 2002.

⁵⁷ Letter from KPMG LLP dated November 25, 2002.

⁵⁸ See, e.g., letter from Deloitte & Touche dated November 27, 2002.

⁵⁹ See, e.g., letter from Robert Waxman dated November 25, 2002.

⁶⁰ Letter from BDO Seidman LLP dated November 25, 2002.

⁶¹ See, e.g., letters from America's Community Bankers dated November 25, 2002, Software Finance & Tax Executives Council dated November 25, 2002, New York State Bar Association dated November 25, 2002, KPMG LLP dated November 25, 2002, and the American Institute of Certified Public Accountants dated November 25, 2002.

⁶² Section 303(a) uses the phrase "independent public or certified accountant," which appears, for example, in items 25, 26 and 27 of Schedule A to the Securities Act of 1933. 15 U.S.C. 77aa(25), (26) and (27). Since the passage of the 1933 Act, however, the general reference to "certified accountant" has been replaced by "certified public accountant." To avoid any possible confusion, we have used "certified public accountant" in the new rules.

⁶³ See section 102 of the Act, which provides that beginning 180 days after the Commission