

financial statements. Commenters, including the European Commission, noted that application of the rule to foreign auditors would place additional and differing layers of retention requirements on those firms.⁸ However, none of the commenters identified any direct conflicts with foreign requirements.

The availability of documents under this rule will assist in the oversight and quality of audits of an issuer's financial statements. Increased retention of identified records also may provide critical evidence of financial reporting impropriety or deficiencies in the audit process. In light of these benefits, and absent a direct conflict with foreign requirements, the retention requirements are to apply equally to domestic and foreign accounting firms auditing the financial statements of foreign issuers. Issues raised by commenters regarding Public Company Accounting Oversight Board ("the Oversight Board") oversight of foreign accounting firms and access by the SEC and the Oversight Board to the records retained by foreign accounting firms, as provided by Section 106 of the Sarbanes-Oxley Act, will be the subject of further discussion among staff, the Commission and the Oversight Board.⁹

In restricting the application of the rule to the audits and reviews of the financial statements of issuers and registered investment companies, we are not condoning more liberal document destruction policies for the audits and reviews of financial statements of other entities. For example, we would expect that auditors of the financial statements of those investment advisers, broker-dealers, and entities subject to Municipal Securities Rulemaking Board regulations that are not subject to the rule would retain relevant audit and review records consistent with applicable laws, regulations, and professional standards.

Documents To Be Retained

Paragraph (a) of rule 2-06 identifies the documents that must be retained and the time period for retaining those documents.¹⁰ The final rule requires

that the auditor¹¹ retain records relevant to the audit or review, including workpapers and other documents that form the basis of the audit or review of an issuer's financial statements, and memoranda, correspondence, communications, other documents, and records (including electronic records) that meet two criteria. The two criteria are that the materials (1) are created, sent or received in connection with the audit or review, and (2) contain conclusions, opinions, analyses, or financial data related to the audit or review.

Paragraph (a) of the proposed rule did not contain the phrase, "records relevant to the audit or review." The proposal listed the records to be retained without a reference to the general notion of relevance to the audit or review. In response to commenters,¹² and to track more closely the wording in section 802,¹³ we have added those words to the final rule.

In the Proposing Release, we stated that non-substantive materials that are not part of the workpapers, such as administrative records, and other documents that do not contain relevant financial data or the auditor's conclusions, opinions or analyses would not meet the second of the criteria in rule 2-06(a) and would not have to be retained. Commentators questioned whether the following documents would be considered substantive and have to be retained:

- Superseded drafts of memoranda, financial statements or regulatory filings,¹⁴
- Notes on superseded drafts of memoranda, financial statements or regulatory filings that reflect incomplete or preliminary thinking,¹⁵
- Previous copies of workpapers that have been corrected for typographical

errors or errors due to training of new employees,¹⁶

- Duplicates of documents,¹⁷ or
- Voice-mail messages.¹⁸

These records generally would not fall within the scope of new rule 2-06 provided they do not contain information or data, relating to a significant matter, that is inconsistent with the auditor's final conclusions, opinions or analyses on that matter or the audit or review.¹⁹ For example, rule 2-06 would require the retention of an item in this list if that item documented a consultation or resolution of differences of professional judgment.

Commenters also questioned whether all of the issuer's financial information, records, databases, and reports that the auditor examines on the issuer's premises, but are not made part of the auditor's workpapers or otherwise currently retained by the auditor, would be deemed to be "received" by the auditor under rule 2-06(a)(1) and have to be retained by the auditor.²⁰ We do not believe that Congress intended for accounting firms to duplicate and retain all of the issuer's financial information, records, databases, and reports that might be read, examined, or reviewed by the auditor. Accordingly, we do not believe that the "received" criterion in rule 2-06(a)(1) requires that such records be retained.

Some commentators suggested that paragraph (a) of the proposed rule was overly broad and that the language in the rule, rather than following section 802 of the Sarbanes-Oxley Act, should conform to current auditing standards.²¹ It would appear, however, that by requiring the retention of documents in addition to audit workpapers required by generally accepted auditing standards ("GAAS") Congress has rejected this approach. Congress intended that accounting firms retain substantive materials that are relevant to

⁸ Letter from the European Commission dated December 20, 2002; letter from PricewaterhouseCoopers dated December 27, 2002; letter from KPMG LLP dated December 27, 2002; letter from the American Institute of Certified Public Accountants dated December 27, 2002.

⁹ We also note that this rule is not intended to expand or restrict the Commission's existing authority to investigate cross-border violations of the federal securities laws.

¹⁰ Rule 2-06 is not intended to pre-empt or supersede any other federal or state record retention requirements.

¹¹ Rule 2-06 uses the term "accountant," which is defined in rule 2-01(f)(1) of the Commission's auditor independence rules, 17 CFR 210.2-01(f)(1), to mean "a certified public accountant or public accountant performing services in connection with an engagement for which independence is required. References to the accountant include any accounting firm with which the certified public or public accountant is affiliated." In a companion release, the Commission proposed to amend this definition to include the term "registered public accounting firm." We will apply the definition in rule 2-01(f)(1), as amended, to rule 2-06.

¹² See, e.g., letter from Deloitte & Touche dated December 27, 2002, and letter from McGladrey & Pullen dated December 31, 2002, which states, in part, "The key to promulgating record retention rules that enhance audit quality lies in the word 'relevant'."

¹³ See note 3, *supra*.

¹⁴ See, e.g., letter from BDO Seidman, LLP, dated December 27, 2002; letter from Ernst & Young LLP, dated December 27, 2002; letter from PricewaterhouseCoopers dated December 27, 2002.

¹⁵ See letter from BDO Seidman, LLP, dated December 27, 2002.

¹⁶ See letter from Gelfond Hochstadt Pangburn, P.C. dated November 26, 2002.

¹⁷ See letter from Ernst & Young LLP, dated December 27, 2002, and letter from Gelfond Hochstadt Pangburn, P.C. dated November 26, 2002.

¹⁸ Letter from Sullivan & Cromwell dated December 26, 2002.

¹⁹ Senator Leahy stated on the Senate floor, "Non-substantive materials, however, which are not relevant to the conclusions or opinions expressed (or not expressed), need not be included in such retention regulations." 148 Cong. Rec. S7419 (July 26, 2002).

²⁰ See, e.g., letter from PricewaterhouseCoopers dated December 27, 2002.

²¹ See, e.g., letter from BDO Seidman, LLP, dated December 27, 2002; letter from Deloitte & Touche dated December 27, 2002; letter from Ernst & Young LLP, dated December 27, 2002; letter from Grant Thornton LLP dated December 27, 2002; letter from KPMG LLP dated December 27, 2002. See the discussion of Statement on Auditing Standards No. 96, "Audit Documentation," *infra*.