

II. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rules

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

A. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rules

(a) Purpose

Section 101(g)(3) of the Act requires the Board to establish ethics rules and standards of conduct for members and staff of the Board. Although the Act does not specify a deadline for the establishment of such rules and standards, the Board recognized that establishing a strict, enforceable Code early in the Board's development would send a strong message to the public that it takes its ethical obligations seriously in pursuing its mission to help restore confidence in issuer audits.

The Code consists of 14 sections (EC 1 through 14). Each section of the Code is discussed below.

Application of Code

EC1 provides that the provisions of the Ethics Code shall apply, according to their terms, to present and former Board members and staff, the spouses, spousal equivalents, and dependents of Board members and staff, and certain contractors and consultants to the Board. A note to the rule cross-references Rule 3700(e), which provides that members of Board advisory groups are subject to certain provisions in the Ethics Code.

EC1. Definitions

EC2 contains definitions of terms used in the Board's Ethics Code.¹

Reference to Rules of the Board

EC2(a) provides that, unless the context requires otherwise, the definitions provided in Section 1001 of the Rules of the Board apply to the words and terms contained in this Ethics Code.

Dependent

EC2(c) defines "dependent" as any person who receives more than half of his or her support for the most recent

calendar year from the Board member or staff. The Ethics Code, as proposed, did not contain a definition of "dependent," but had defined the term "immediate family." Two commenters recommended that the Board adopt a definition of "immediate family" that more closely resembles the Commission's definition of "immediate family member" in its auditor independence rules. The Commission's definition of "immediate family" covers an individual's "spouse, spousal equivalent, and dependents."²

The Board agreed, in principle, with this recommendation. To promote clarity, however, the Board eliminated its use of the defined term "immediate family" and added "spouse, spousal equivalent, and dependents" directly to those provisions of the Ethics Code that previously used the defined term "immediate family." While the Board only included a definition, based on the Commission's interpretation of Regulation S-X, for "dependent," the Board will interpret each of these terms in a manner consistent with how they are used in the Commission's Regulation S-X definition.³ Accordingly, "spouse" will mean husband or wife, whether by marriage or common law, and "spousal equivalent" will mean cohabitant occupying a relationship generally equivalent to that of a spouse.

While the definition of "dependent" applies equally to minor or adult dependents, depending on their receipt of support from the Board or staff member, there may be situations in which it might be appropriate for the Ethics Code to apply differently in the case of an adult dependent who does not reside with the Board or staff member. If appropriate and consistent with EC13, the Board envisions that the Board's Ethics Officer or other person to whom the Board delegates waiver authority with regard to staff will recommend a waiver in such situations.

Designated Contractors and Consultants

EC2(d) defines the term "designated contractors and consultants" as those persons or business organizations with whom the Board enters into contracts for services, whom the Board (or its designate) determines should be subject to the Code, and for which the contract contains a provision expressly incorporating this Code (in whole or in

part). The Board will develop and maintain a list of designated contractors and consultants, which will be available to the public and will reserve the right to contractually impose additional restrictions and limitations on any contractor or consultant.

Two commenters indicated that they believed the original definition was overly vague and could apply to all providers of goods and services to the Board. The proposing release provided a two-part test for designated contractors and consultants. It indicated that designated contractors and consultants are those persons with whom the Board entered into contracts for services and for which the contracts expressly incorporated the Code, in whole or in part. Based upon these concerns, the Board added a third criterion—a requirement that the Board determine, on a case-by-case basis, whether, and to what degree, each contractor or consultant should be subject to the Code.

Honoraria

EC2(e) defines "honoraria" as anything with more than a nominal value, whether provided in cash or otherwise, and which is provided in exchange for a speech, panel participation, publication or lecture. EC2(e) further indicates that neither the waiver or conference fee, nor the acceptance of a modest speakers-only meal shall constitute honoraria. "Nominal value" will initially be interpreted to mean fair market value of \$50 or less.

Practice

EC2(f) defines "practice" as it relates to activities before the Board or Commission. Subparagraph (1) of the definition provides that practice means knowingly acting as an agent or attorney for, or otherwise representing any person (other than oneself) in any formal or informal appearance before the Board or Commission. Subparagraph (2) provides an alternative meaning, indicating that practice also means making any oral or written communication on behalf of any person (other than oneself) to, and with the intent to influence, the Board or Commission.

This definition, as incorporated in EC12(b), is intended to restrict affected persons from certain representational activities. However, this definition, as incorporated by EC12(b), is not intended to prevent affected persons from participating in the preparation of documents, communications, presentations or the like, provided the affected persons do not appear before, or

² See Rule 2-01(f)(13) of Regulation S-X, 17 CFR 210.1-01(f)(13).

³ See Commission Final Rule: Revision of the Commission's Auditor Independence Requirements, Release No. 33-7919 (November 21, 2000) (describing these terms in the context of the rule's definition of "close family members").

¹ Certain definitions in the Board's rules that are self-explanatory are not discussed below.