

Securities and Exchange Commission

§ 210.2-01

QUALIFICATIONS AND REPORTS OF ACCOUNTANTS

SOURCE: Sections 210.2-01 through 210.2-05 appear at 37 FR 14594, July 21, 1972, unless otherwise noted.

§ 210.2-01 Qualifications of accountants.

Preliminary Note to § 210.2-01

1. Section 210.2-01 is designed to ensure that auditors are qualified and independent of their audit clients both in fact and in appearance. Accordingly, the rule sets forth restrictions on financial, employment, and business relationships between an accountant and an audit client and restrictions on an accountant providing certain non-audit services to an audit client.

2. Section 210.2-01(b) sets forth the general standard of auditor independence. Paragraphs (c)(1) to (c)(5) reflect the application of the general standard to particular circumstances. The rule does not purport to, and the Commission could not, consider all circumstances that raise independence concerns, and these are subject to the general standard in § 210.2-01(b). In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service: creates a mutual or conflicting interest between the accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client.

3. These factors are general guidance only and their application may depend on particular facts and circumstances. For that reason, § 210.2-01 provides that, in determining whether an accountant is independent, the Commission will consider all relevant facts and circumstances. For the same reason, registrants and accountants are encouraged to consult with the Commission's Office of the Chief Accountant before entering into relationships, including relationships involving the provision of services, that are not explicitly described in the rule.

(a) The Commission will not recognize any person as a certified public accountant who is not duly registered and in good standing as such under the laws of the place of his residence or principal office. The Commission will not recognize any person as a public accountant who is not in good standing and entitled to practice as such under the laws of the place of his residence or principal office.

(b) The Commission will not recognize an accountant as independent, with respect to an audit client, if the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement. In determining whether an accountant is independent, the Commission will consider all relevant circumstances, including all relationships between the accountant and the audit client, and not just those relating to reports filed with the Commission.

(c) This paragraph sets forth a non-exclusive specification of circumstances inconsistent with paragraph (b) of this section.

(1) *Financial relationships.* An accountant is not independent if, at any point during the audit and professional engagement period, the accountant has a direct financial interest or a material indirect financial interest in the accountant's audit client, such as:

(i) *Investments in audit clients.* An accountant is not independent when:

(A) The accounting firm, any covered person in the firm, or any of his or her immediate family members, has any direct investment in an audit client, such as stocks, bonds, notes, options, or other securities. The term *direct investment* includes an investment in an audit client through an intermediary if:

(1) The accounting firm, covered person, or immediate family member, alone or together with other persons, supervises or participates in the intermediary's investment decisions or has control over the intermediary; or

(2) The intermediary is not a diversified management investment company, as defined by section 5(b)(1) of the Investment Company Act of 1940, 15 U.S.C. 80a-5(b)(1), and has an investment in the audit client that amounts to 20% or more of the value of the intermediary's total investments.

(B) Any partner, principal, shareholder, or professional employee of the accounting firm, any of his or her immediate family members, any close family member of a covered person in

the firm, or any group of the above persons has filed a Schedule 13D or 13G (17 CFR 240.13d-101 or 240.13d-102) with the Commission indicating beneficial ownership of more than five percent of an audit client's equity securities or controls an audit client, or a close family member of a partner, principal, or shareholder of the accounting firm controls an audit client.

(C) The accounting firm, any covered person in the firm, or any of his or her immediate family members, serves as voting trustee of a trust, or executor of an estate, containing the securities of an audit client, unless the accounting firm, covered person in the firm, or immediate family member has no authority to make investment decisions for the trust or estate.

(D) The accounting firm, any covered person in the firm, any of his or her immediate family members, or any group of the above persons has any material indirect investment in an audit client. For purposes of this paragraph, the term *material indirect investment* does not include ownership by any covered person in the firm, any of his or her immediate family members, or any group of the above persons of 5% or less of the outstanding shares of a diversified management investment company, as defined by section 5(b)(1) of the Investment Company Act of 1940, 15 U.S.C. 80a-5(b)(1), that invests in an audit client.

(E) The accounting firm, any covered person in the firm, or any of his or her immediate family members:

(1) Has any direct or material indirect investment in an entity where:

(i) An audit client has an investment in that entity that is material to the audit client and has the ability to exercise significant influence over that entity; or

(ii) The entity has an investment in an audit client that is material to that entity and has the ability to exercise significant influence over that audit client;

(2) Has any material investment in an entity over which an audit client has the ability to exercise significant influence; or

(3) Has the ability to exercise significant influence over an entity that has

the ability to exercise significant influence over an audit client.

(ii) *Other financial interests in audit client.* An accountant is not independent when the accounting firm, any covered person in the firm, or any of his or her immediate family members has:

(A) *Loans/debtor-creditor relationship.* Any loan (including any margin loan) to or from an audit client, or an audit client's officers, directors, or record or beneficial owners of more than ten percent of the audit client's equity securities, except for the following loans obtained from a financial institution under its normal lending procedures, terms, and requirements:

(1) Automobile loans and leases collateralized by the automobile;

(2) Loans fully collateralized by the cash surrender value of an insurance policy;

(3) Loans fully collateralized by cash deposits at the same financial institution; and

(4) A mortgage loan collateralized by the borrower's primary residence provided the loan was not obtained while the covered person in the firm was a covered person.

(B) *Savings and checking accounts.* Any savings, checking, or similar account at a bank, savings and loan, or similar institution that is an audit client, if the account has a balance that exceeds the amount insured by the Federal Deposit Insurance Corporation or any similar insurer, except that an accounting firm account may have an uninsured balance provided that the likelihood of the bank, savings and loan, or similar institution experiencing financial difficulties is remote.

(C) *Broker-dealer accounts.* Brokerage or similar accounts maintained with a broker-dealer that is an audit client, if:

(1) Any such account includes any asset other than cash or securities (within the meaning of "security" provided in the Securities Investor Protection Act of 1970 ("SIPA") (15 U.S.C. 78aaa *et seq.*));

(2) The value of assets in the accounts exceeds the amount that is subject to a Securities Investor Protection Corporation advance, for those accounts, under Section 9 of SIPA (15 U.S.C. 78fff-3); or

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(3) With respect to non-U.S. accounts not subject to SIPA protection, the value of assets in the accounts exceeds the amount insured or protected by a program similar to SIPA.

(D) *Futures commission merchant accounts.* Any futures, commodity, or similar account maintained with a futures commission merchant that is an audit client.

(E) *Credit cards.* Any aggregate outstanding credit card balance owed to a lender that is an audit client that is not reduced to \$10,000 or less on a current basis taking into consideration the payment due date and any available grace period.

(F) *Insurance products.* Any individual policy issued by an insurer that is an audit client unless:

(1) The policy was obtained at a time when the covered person in the firm was not a covered person in the firm; and

(2) The likelihood of the insurer becoming insolvent is remote.

(G) *Investment companies.* Any financial interest in an entity that is part of an investment company complex that includes an audit client.

(iii) *Exceptions.* Notwithstanding paragraphs (c)(1)(i) and (c)(1)(ii) of this section, an accountant will not be deemed not independent if:

(A) *Inheritance and gift.* Any person acquires an unsolicited financial interest, such as through an unsolicited gift or inheritance, that would cause an accountant to be not independent under paragraph (c)(1)(i) or (c)(1)(ii) of this section, and the financial interest is disposed of as soon as practicable, but no later than 30 days after the person has knowledge of and the right to dispose of the financial interest.

(B) *New audit engagement.* Any person has a financial interest that would cause an accountant to be not independent under paragraph (c)(1)(i) or (c)(1)(ii) of this section, and:

(1) The accountant did not audit the client's financial statements for the immediately preceding fiscal year; and

(2) The accountant is independent under paragraph (c)(1)(i) and (c)(1)(ii) of this section before the earlier of:

(i) Signing an initial engagement letter or other agreement to provide

audit, review, or attest services to the audit client; or

(ii) Commencing any audit, review, or attest procedures (including planning the audit of the client's financial statements).

(C) *Employee compensation and benefit plans.* An immediate family member of a person who is a covered person in the firm only by virtue of paragraphs (f)(11)(iii) or (f)(11)(iv) of this section has a financial interest that would cause an accountant to be not independent under paragraph (c)(1)(i) or (c)(1)(ii) of this section, and the acquisition of the financial interest was an unavoidable consequence of participation in his or her employer's employee compensation or benefits program, provided that the financial interest, other than unexercised employee stock options, is disposed of as soon as practicable, but no later than 30 days after the person has the right to dispose of the financial interest.

(iv) *Audit clients' financial relationships.* An accountant is not independent when:

(A) *Investments by the audit client in the accounting firm.* An audit client has, or has agreed to acquire, any direct investment in the accounting firm, such as stocks, bonds, notes, options, or other securities, or the audit client's officers or directors are record or beneficial owners of more than 5% of the equity securities of the accounting firm.

(B) *Underwriting.* An accounting firm engages an audit client to act as an underwriter, broker-dealer, market-maker, promoter, or analyst with respect to securities issued by the accounting firm.

(2) *Employment relationships.* An accountant is not independent if, at any point during the audit and professional engagement period, the accountant has an employment relationship with an audit client, such as:

(i) *Employment at audit client of accountant.* A current partner, principal, shareholder, or professional employee of the accounting firm is employed by the audit client or serves as a member of the board of directors or similar management or governing body of the audit client.

(ii) *Employment at audit client of certain relatives of accountant.* A close family member of a covered person in the firm is in an accounting role or financial reporting oversight role at an audit client, or was in such a role during any period covered by an audit for which the covered person in the firm is a covered person.

(iii) *Employment at audit client of former employee of accounting firm.* (A) A former partner, principal, shareholder, or professional employee of an accounting firm is in an accounting role or financial reporting oversight role at an audit client, unless the individual:

(1) Does not influence the accounting firm's operations or financial policies;

(2) Has no capital balances in the accounting firm; and

(3) Has no financial arrangement with the accounting firm other than one providing for regular payment of a fixed dollar amount (which is not dependent on the revenues, profits, or earnings of the accounting firm):

(i) Pursuant to a fully funded retirement plan, rabbi trust, or, in jurisdictions in which a rabbi trust does not exist, a similar vehicle; or

(ii) In the case of a former professional employee who was not a partner, principal, or shareholder of the accounting firm and who has been disassociated from the accounting firm for more than five years, that is immaterial to the former professional employee; and

(B) A former partner, principal, shareholder, or professional employee of an accounting firm is in a financial reporting oversight role at an issuer (as defined in section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f)), except an issuer that is an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), unless the individual:

(1) Employed by the issuer was not a member of the audit engagement team of the issuer during the one year period preceding the date that audit procedures commenced for the fiscal period that included the date of initial employment of the audit engagement team member by the issuer;

(2) For purposes of paragraph (c)(2)(iii)(B)(1) of this section, the fol-

lowing individuals are not considered to be members of the audit engagement team:

(i) Persons, other than the lead partner and the concurring partner, who provided ten or fewer hours of audit, review, or attest services during the period covered by paragraph (c)(2)(iii)(B)(1) of this section;

(ii) Individuals employed by the issuer as a result of a business combination between an issuer that is an audit client and the employing entity, provided employment was not in contemplation of the business combination and the audit committee of the successor issuer is aware of the prior employment relationship; and

(iii) Individuals that are employed by the issuer due to an emergency or other unusual situation provided that the audit committee determines that the relationship is in the interest of investors;

(3) For purposes of paragraph (c)(2)(iii)(B)(1) of this section, audit procedures are deemed to have commenced for a fiscal period the day following the filing of the issuer's periodic annual report with the Commission covering the previous fiscal period; or

(C) A former partner, principal, shareholder, or professional employee of an accounting firm is in a financial reporting oversight role with respect to an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), if:

(1) The former partner, principal, shareholder, or professional employee of an accounting firm is employed in a financial reporting oversight role related to the operations and financial reporting of the registered investment company at an entity in the investment company complex, as defined in (f)(14) of this section, that includes the registered investment company; and

(2) The former partner, principal, shareholder, or professional employee of an accounting firm employed by the registered investment company or any entity in the investment company complex was a member of the audit engagement team of the registered investment company or any other registered investment company in the investment company complex during the

one year period preceding the date that audit procedures commenced that included the date of initial employment of the audit engagement team member by the registered investment company or any entity in the investment company complex.

(3) For purposes of paragraph (c)(2)(iii)(C)(2) of this section, the following individuals are not considered to be members of the audit engagement team:

(i) Persons, other than the lead partner and concurring partner, who provided ten or fewer hours of audit, review or attest services during the period covered by paragraph (c)(2)(iii)(C)(2) of this section;

(ii) Individuals employed by the registered investment company or any entity in the investment company complex as a result of a business combination between a registered investment company or any entity in the investment company complex that is an audit client and the employing entity, provided employment was not in contemplation of the business combination and the audit committee of the registered investment company is aware of the prior employment relationship; and

(iii) Individuals that are employed by the registered investment company or any entity in the investment company complex due to an emergency or other unusual situation provided that the audit committee determines that the relationship is in the interest of investors.

(4) For purposes of paragraph (c)(2)(iii)(C)(2) of this section, audit procedures are deemed to have commenced the day following the filing of the registered investment company's periodic annual report with the Commission.

(iv) *Employment at accounting firm of former employee of audit client.* A former officer, director, or employee of an audit client becomes a partner, principal, shareholder, or professional employee of the accounting firm, unless the individual does not participate in, and is not in a position to influence, the audit of the financial statements of the audit client covering any period during which he or she was employed by or associated with that audit client.

(3) *Business relationships.* An accountant is not independent if, at any point during the audit and professional engagement period, the accounting firm or any covered person in the firm has any direct or material indirect business relationship with an audit client, or with persons associated with the audit client in a decision-making capacity, such as an audit client's officers, directors, or substantial stockholders. The relationships described in this paragraph do not include a relationship in which the accounting firm or covered person in the firm provides professional services to an audit client or is a consumer in the ordinary course of business.

(4) *Non-audit services.* An accountant is not independent if, at any point during the audit and professional engagement period, the accountant provides the following non-audit services to an audit client:

(i) *Bookkeeping or other services related to the accounting records or financial statements of the audit client.* Any service, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements, including:

(A) Maintaining or preparing the audit client's accounting records;

(B) Preparing the audit client's financial statements that are filed with the Commission or that form the basis of financial statements filed with the Commission; or

(C) Preparing or originating source data underlying the audit client's financial statements.

(ii) *Financial information systems design and implementation.* Any service, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements, including:

(A) Directly or indirectly operating, or supervising the operation of, the audit client's information system or managing the audit client's local area network; or

(B) Designing or implementing a hardware or software system that aggregates source data underlying the financial statements or generates information that is significant to the audit

client's financial statements or other financial information systems taken as a whole.

(iii) *Appraisal or valuation services, fairness opinions, or contribution-in-kind reports.* Any appraisal service, valuation service, or any service involving a fairness opinion or contribution-in-kind report for an audit client, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements.

(iv) *Actuarial services.* Any actuarially-oriented advisory service involving the determination of amounts recorded in the financial statements and related accounts for the audit client other than assisting a client in understanding the methods, models, assumptions, and inputs used in computing an amount, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements.

(v) *Internal audit outsourcing services.* Any internal audit service that has been outsourced by the audit client that relates to the audit client's internal accounting controls, financial systems, or financial statements, for an audit client unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements.

(vi) *Management functions.* Acting, temporarily or permanently, as a director, officer, or employee of an audit client, or performing any decision-making, supervisory, or ongoing monitoring function for the audit client.

(vii) *Human resources.* (A) Searching for or seeking out prospective candidates for managerial, executive, or director positions;

(B) Engaging in psychological testing, or other formal testing or evaluation programs;

(C) Undertaking reference checks of prospective candidates for an executive or director position;

(D) Acting as a negotiator on the audit client's behalf, such as determining position, status or title, compensation, fringe benefits, or other conditions of employment; or

(E) Recommending, or advising the audit client to hire, a specific candidate for a specific job (except that an accounting firm may, upon request by the audit client, interview candidates and advise the audit client on the candidate's competence for financial accounting, administrative, or control positions).

(viii) *Broker-dealer, investment adviser, or investment banking services.* Acting as a broker-dealer (registered or unregistered), promoter, or underwriter, on behalf of an audit client, making investment decisions on behalf of the audit client or otherwise having discretionary authority over an audit client's investments, executing a transaction to buy or sell an audit client's investment, or having custody of assets of the audit client, such as taking temporary possession of securities purchased by the audit client.

(ix) *Legal services.* Providing any service to an audit client that, under circumstances in which the service is provided, could be provided only by someone licensed, admitted, or otherwise qualified to practice law in the jurisdiction in which the service is provided.

(x) *Expert services unrelated to the audit.* Providing an expert opinion or other expert service for an audit client, or an audit client's legal representative, for the purpose of advocating an audit client's interests in litigation or in a regulatory or administrative proceeding or investigation. In any litigation or regulatory or administrative proceeding or investigation, an accountant's independence shall not be deemed to be impaired if the accountant provides factual accounts, including in testimony, of work performed or explains the positions taken or conclusions reached during the performance of any service provided by the accountant for the audit client.

(5) *Contingent fees.* An accountant is not independent if, at any point during the audit and professional engagement period, the accountant provides any service or product to an audit client for a contingent fee or a commission, or receives a contingent fee or commission from an audit client.

(6) *Partner rotation.* (i) Except as provided in paragraph (c)(6)(ii) of this section, an accountant is not independent of an audit client when:

(A) Any audit partner as defined in paragraph (f)(7)(ii) of this section performs:

(1) The services of a lead partner, as defined in paragraph (f)(7)(ii)(A) of this section, or concurring partner, as defined in paragraph (f)(7)(ii)(B) of this section, for more than five consecutive years; or

(2) One or more of the services defined in paragraphs (f)(7)(ii)(C) and (D) of this section for more than seven consecutive years;

(B) Any audit partner:

(1) Within the five consecutive year period following the performance of services for the maximum period permitted under paragraph (c)(6)(i)(A)(1) of this section, performs for that audit client the services of a lead partner, as defined in paragraph (f)(7)(ii)(A) of this section, or concurring partner, as defined in paragraph (f)(7)(ii)(B) of this section, or a combination of those services, or

(2) Within the two consecutive year period following the performance of services for the maximum period permitted under paragraph (c)(6)(i)(A)(2) of this section, performs one or more of the services defined in paragraph (f)(7)(ii) of this section.

(ii) Any accounting firm with less than five audit clients that are issuers (as defined in section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f))) and less than ten partners shall be exempt from paragraph (c)(6)(i) of this section *provided* the Public Company Accounting Oversight Board conducts a review at least once every three years of each of the audit client engagements that would result in a lack of auditor independence under this paragraph.

(iii) For purposes of paragraph (c)(6)(i) of this section, an audit client that is an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), does not include an affiliate of the audit client that is an entity in the same investment company complex, as defined in paragraph (f)(14) of this section, except for another registered in-

vestment company in the same investment company complex. For purposes of calculating consecutive years of service under paragraph (c)(6)(i) of this section with respect to investment companies in an investment company complex, audits of registered investment companies with different fiscal year-ends that are performed in a continuous 12-month period count as a single consecutive year.

(7) *Audit committee administration of the engagement.* An accountant is not independent of an issuer (as defined in section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f))), other than an issuer that is an Asset-Backed Issuer as defined in § 229.1101 of this chapter, or an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), other than a unit investment trust as defined by section 4(2) of the Investment Company Act of 1940 (15 U.S.C. 80a-4(2)), unless:

(i) In accordance with Section 10A(i) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(i)) either:

(A) Before the accountant is engaged by the issuer or its subsidiaries, or the registered investment company or its subsidiaries, to render audit or non-audit services, the engagement is approved by the issuer's or registered investment company's audit committee; or

(B) The engagement to render the service is entered into pursuant to pre-approval policies and procedures established by the audit committee of the issuer or registered investment company, *provided* the policies and procedures are detailed as to the particular service and the audit committee is informed of each service and such policies and procedures do not include delegation of the audit committees responsibilities under the Securities Exchange Act of 1934 to management; or

(C) With respect to the provision of services other than audit, review or attest services the pre-approval requirement is waived if:

(1) The aggregate amount of all such services provided constitutes no more than five percent of the total amount of revenues paid by the audit client to its accountant during the fiscal year in which the services are provided;

(2) Such services were not recognized by the issuer or registered investment company at the time of the engagement to be non-audit services; and

(3) Such services are promptly brought to the attention of the audit committee of the issuer or registered investment company and approved prior to the completion of the audit by the audit committee or by one or more members of the audit committee who are members of the board of directors to whom authority to grant such approvals has been delegated by the audit committee.

(ii) A registered investment company's audit committee also must pre-approve its accountant's engagements for non-audit services with the registered investment company's investment adviser (not including a sub-adviser whose role is primarily portfolio management and is sub-contracted or overseen by another investment adviser) and any entity controlling, controlled by, or under common control with the investment adviser that provides ongoing services to the registered investment company in accordance with paragraph (c)(7)(i) of this section, if the engagement relates directly to the operations and financial reporting of the registered investment company, except that with respect to the waiver of the pre-approval requirement under paragraph (c)(7)(i)(C) of this section, the aggregate amount of all services provided constitutes no more than five percent of the total amount of revenues paid to the registered investment company's accountant by the registered investment company, its investment adviser and any entity controlling, controlled by, or under common control with the investment adviser that provides ongoing services to the registered investment company during the fiscal year in which the services are provided that would have to be pre-approved by the registered investment company's audit committee pursuant to this section.

(8) *Compensation.* An accountant is not independent of an audit client if, at any point during the audit and professional engagement period, any audit partner earns or receives compensation based on the audit partner procuring engagements with that audit client to

provide any products or services other than audit, review or attest services. Any accounting firm with fewer than ten partners and fewer than five audit clients that are issuers (as defined in section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f))) shall be exempt from the requirement stated in the previous sentence.

(d) *Quality controls.* An accounting firm's independence will not be impaired solely because a covered person in the firm is not independent of an audit client provided:

(1) The covered person did not know of the circumstances giving rise to the lack of independence;

(2) The covered person's lack of independence was corrected as promptly as possible under the relevant circumstances after the covered person or accounting firm became aware of it; and

(3) The accounting firm has a quality control system in place that provides reasonable assurance, taking into account the size and nature of the accounting firm's practice, that the accounting firm and its employees do not lack independence, and that covers at least all employees and associated entities of the accounting firm participating in the engagement, including employees and associated entities located outside of the United States.

(4) For an accounting firm that annually provides audit, review, or attest services to more than 500 companies with a class of securities registered with the Commission under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l), a quality control system will not provide such reasonable assurance unless it has at least the following features:

(i) Written independence policies and procedures;

(ii) With respect to partners and managerial employees, an automated system to identify their investments in securities that might impair the accountant's independence;

(iii) With respect to all professionals, a system that provides timely information about entities from which the accountant is required to maintain independence;

(iv) An annual or on-going firm-wide training program about auditor independence;

(v) An annual internal inspection and testing program to monitor adherence to independence requirements;

(vi) Notification to all accounting firm members, officers, directors, and employees of the name and title of the member of senior management responsible for compliance with auditor independence requirements;

(vii) Written policies and procedures requiring all partners and covered persons to report promptly to the accounting firm when they are engaged in employment negotiations with an audit client, and requiring the firm to remove immediately any such professional from that audit client's engagement and to review promptly all work the professional performed related to that audit client's engagement; and

(viii) A disciplinary mechanism to ensure compliance with this section.

(e)(1) *Transition and grandfathering.* Provided the following relationships did not impair the accountant's independence under pre-existing requirements of the Commission, the Independence Standards Board, or the accounting profession in the United States, the existence of the relationship on May 6, 2003 will not be deemed to impair an accountant's independence:

(i) Employment relationships that commenced at the issuer prior to May 6, 2003 as described in paragraph (c)(2)(iii)(B) of this section.

(ii) Compensation earned or received, as described in paragraph (c)(8) of this section during the fiscal year of the accounting firm that includes the effective date of this section.

(iii) Until May 6, 2004, the provision of services described in paragraph (c)(4) of this section provided those services are pursuant to contracts in existence on May 6, 2003.

(iv) The provision of services by the accountant under contracts in existence on May 6, 2003 that have not been pre-approved by the audit committee as described in paragraph (c)(7) of this section.

(v) Until the first day of the issuer's fiscal year beginning after May 6, 2003 by a "lead" partner and other audit

partner (other than the "concurring" partner) providing services in excess of those permitted under paragraph (c)(6) of this section. An accountant's independence will not be deemed to be impaired until the first day of the issuer's fiscal year beginning after May 6, 2004 by a "concurring" partner providing services in excess of those permitted under paragraph (c)(6) of this section. For the purposes of calculating periods of service under paragraph (c)(6) of this section:

(A) For the "lead" and "concurring" partner, the period of service includes time served as the "lead" or "concurring" partner prior to May 6, 2003; and

(B) For audit partners other than the "lead" partner or "concurring" partner, and for audit partners in foreign firms, the period of service does not include time served on the audit engagement team prior to the first day of issuer's fiscal year beginning on or after May 6, 2003.

(2) *Settling financial arrangements with former professionals.* To the extent not required by pre-existing requirements of the Commission, the Independence Standards Board, or the accounting profession in the United States, the requirement in paragraph (c)(2)(iii) of this section to settle financial arrangements with former professionals applies to situations that arise after the effective date of this section.

(f) *Definitions of terms.* For purposes of this section:

(1) *Accountant*, as used in paragraphs (b) through (e) of this section, means a registered public accounting firm, 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 accountant or public accountant is affiliated.

(2) *Accounting firm* means an organization (whether it is a sole proprietorship, incorporated association, partnership, corporation, limited liability company, limited liability partnership, or other legal entity) that is engaged in the practice of public accounting and furnishes reports or other documents filed with the Commission or otherwise prepared under the securities

laws, and all of the organization's departments, divisions, parents, subsidiaries, and associated entities, including those located outside of the United States. Accounting firm also includes the organization's pension, retirement, investment, or similar plans.

(3)(i) *Accounting role* means a role in which a person is in a position to or does exercise more than minimal influence over the contents of the accounting records or anyone who prepares them.

(ii) *Financial reporting oversight role* means a role in which a person is in a position to or does exercise influence over the contents of the financial statements or anyone who prepares them, such as when the person is a member of the board of directors or similar management or governing body, chief executive officer, president, chief financial officer, chief operating officer, general counsel, chief accounting officer, controller, director of internal audit, director of financial reporting, treasurer, or any equivalent position.

(4) *Affiliate of the audit client* means:

(i) An entity that has control over the audit client, or over which the audit client has control, or which is under common control with the audit client, including the audit client's parents and subsidiaries;

(ii) An entity over which the audit client has significant influence, unless the entity is not material to the audit client;

(iii) An entity that has significant influence over the audit client, unless the audit client is not material to the entity; and

(iv) Each entity in the investment company complex when the audit client is an entity that is part of an investment company complex.

(5) *Audit and professional engagement period* includes both:

(i) The period covered by any financial statements being audited or reviewed (the "audit period"); and

(ii) The period of the engagement to audit or review the audit client's financial statements or to prepare a report filed with the Commission (the "professional engagement period");

(A) The professional engagement period begins when the accountant either

signs an initial engagement letter (or other agreement to review or audit a client's financial statements) or begins audit, review, or attest procedures, whichever is earlier; and

(B) The professional engagement period ends when the audit client or the accountant notifies the Commission that the client is no longer that accountant's audit client.

(iii) For audits of the financial statements of foreign private issuers, the "audit and professional engagement period" does not include periods ended prior to the first day of the last fiscal year before the foreign private issuer first filed, or was required to file, a registration statement or report with the Commission, provided there has been full compliance with home country independence standards in all prior periods covered by any registration statement or report filed with the Commission.

(6) *Audit client* means the entity whose financial statements or other information is being audited, reviewed, or attested and any affiliates of the audit client, other than, for purposes of paragraph (c)(1)(i) of this section, entities that are affiliates of the audit client only by virtue of paragraph (f)(4)(ii) or (f)(4)(iii) of this section.

(7)(i) *Audit engagement team* means all partners, principals, shareholders and professional employees participating in an audit, review, or attestation engagement of an audit client, including audit partners and all persons who consult with others on the audit engagement team during the audit, review, or attestation engagement regarding technical or industry-specific issues, transactions, or events.

(ii) *Audit partner* means a partner or persons in an equivalent position, other than a partner who consults with others on the audit engagement team during the audit, review, or attestation engagement regarding technical or industry-specific issues, transactions, or events, who is a member of the audit engagement team who has responsibility for decision-making on significant auditing, accounting, and reporting matters that affect the financial statements, or who maintains regular contact with management and the

audit committee and includes the following:

(A) The lead or coordinating audit partner having primary responsibility for the audit or review (the “lead partner”);

(B) The partner performing a second level of review to provide additional assurance that the financial statements subject to the audit or review are in conformity with generally accepted accounting principles and the audit or review and any associated report are in accordance with generally accepted auditing standards and rules promulgated by the Commission or the Public Company Accounting Oversight Board (the “concurring or reviewing partner”);

(C) Other audit engagement team partners who provide more than ten hours of audit, review, or attest services in connection with the annual or interim consolidated financial statements of the issuer or an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8); and

(D) Other audit engagement team partners who serve as the “lead partner” in connection with any audit or review related to the annual or interim financial statements of a subsidiary of the issuer whose assets or revenues constitute 20% or more of the assets or revenues of the issuer’s respective consolidated assets or revenues.

(8) *Chain of command* means all persons who:

(i) Supervise or have direct management responsibility for the audit, including at all successively senior levels through the accounting firm’s chief executive;

(ii) Evaluate the performance or recommend the compensation of the audit engagement partner; or

(iii) Provide quality control or other oversight of the audit.

(9) *Close family members* means a person’s spouse, spousal equivalent, parent, dependent, nondependent child, and sibling.

(10) *Contingent fee* means, except as stated in the next sentence, any fee established for the sale of a product or the performance of any service pursuant to an arrangement in which no fee will be charged unless a specified finding or result is attained, or in which

the amount of the fee is otherwise dependent upon the finding or result of such product or service. Solely for the purposes of this section, a fee is not a “contingent fee” if it is fixed by courts or other public authorities, or, in tax matters, if determined based on the results of judicial proceedings or the findings of governmental agencies. Fees may vary depending, for example, on the complexity of services rendered.

(11) *Covered persons in the firm* means the following partners, principals, shareholders, and employees of an accounting firm:

(i) The “audit engagement team”;

(ii) The “chain of command”;

(iii) Any other partner, principal, shareholder, or managerial employee of the accounting firm who has provided ten or more hours of non-audit services to the audit client for the period beginning on the date such services are provided and ending on the date the accounting firm signs the report on the financial statements for the fiscal year during which those services are provided, or who expects to provide ten or more hours of non-audit services to the audit client on a recurring basis; and

(iv) Any other partner, principal, or shareholder from an “office” of the accounting firm in which the lead audit engagement partner primarily practices in connection with the audit.

(12) *Group* means two or more persons who act together for the purposes of acquiring, holding, voting, or disposing of securities of a registrant.

(13) *Immediate family members* means a person’s spouse, spousal equivalent, and dependents.

(14) *Investment company complex*. (i) “Investment company complex” includes:

(A) An investment company and its investment adviser or sponsor;

(B) Any entity controlled by or controlling an investment adviser or sponsor in paragraph (f)(14)(i)(A) of this section, or any entity under common control with an investment adviser or sponsor in paragraph (f)(14)(i)(A) of this section if the entity:

(1) Is an investment adviser or sponsor; or

(2) Is engaged in the business of providing administrative, custodian, underwriting, or transfer agent services

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to any investment company, investment adviser, or sponsor; and

(C) Any investment company or entity that would be an investment company but for the exclusions provided by section 3(c) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(c)) that has an investment adviser or sponsor included in this definition by either paragraph (f)(14)(i)(A) or (f)(14)(i)(B) of this section.

(ii) An investment adviser, for purposes of this definition, does not include a sub-adviser whose role is primarily portfolio management and is subcontracted with or overseen by another investment adviser.

(iii) Sponsor, for purposes of this definition, is an entity that establishes a unit investment trust.

(15) *Office* means a distinct sub-group within an accounting firm, whether distinguished along geographic or practice lines.

(16) *Rabbi trust* means an irrevocable trust whose assets are not accessible to the accounting firm until all benefit obligations have been met, but are subject to the claims of creditors in bankruptcy or insolvency.

(17) *Audit committee* means a committee (or equivalent body) as defined in section 3(a)(58) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(58)).

[37 FR 14594, July 21, 1972, as amended at 48 FR 9521, Mar. 7, 1983; 65 FR 76082, Dec. 5, 2000; 68 FR 6044, Feb. 5, 2003; 70 FR 1593, Jan. 7, 2005]

§210.2-02 Accountants' reports and attestation reports.

(a) *Technical requirements for accountants' reports.* The accountant's report:

- (1) Shall be dated;
- (2) Shall be signed manually;
- (3) Shall indicate the city and State where issued; and
- (4) Shall identify without detailed enumeration the financial statements covered by the report.

(b) *Representations as to the audit included in accountants' reports.* The accountant's report:

- (1) Shall state whether the audit was made in accordance with generally accepted auditing standards; and
- (2) Shall designate any auditing procedures deemed necessary by the accountant under the circumstances of

the particular case, which have been omitted, and the reasons for their omission. Nothing in this rule shall be construed to imply authority for the omission of any procedure which independent accountants would ordinarily employ in the course of an audit made for the purpose of expressing the opinions required by paragraph (c) of this section.

(c) *Opinions to be expressed in accountants' reports.* The accountant's report shall state clearly:

(1) The opinion of the accountant in respect of the financial statements covered by the report and the accounting principles and practices reflected therein; and

(2) The opinion of the accountant as to the consistency of the application of the accounting principles, or as to any changes in such principles which have a material effect on the financial statements.

(d) *Exceptions identified in accountants' reports.* Any matters to which the accountant takes exception shall be clearly identified, the exception thereto specifically and clearly stated, and, to the extent practicable, the effect of each such exception on the related financial statements given. (See section 101 of the Codification of Financial Reporting Policies.)

(e) Paragraph (e) of this section applies only to registrants that are providing financial statements in a filing for a period with respect to which Arthur Andersen LLP or a foreign affiliate of Arthur Andersen LLP ("Andersen") issued an accountants' report. Notwithstanding any other Commission rule or regulation, a registrant that cannot obtain an accountants' report that meets the technical requirements of paragraph (a) of this section after reasonable efforts may include in the document a copy of the latest signed and dated accountants' report issued by Andersen for such period in satisfaction of that requirement, if prominent disclosure that the report is a copy of the previously issued Andersen accountants' report and that the report has not been reissued by Andersen is set forth on such copy.

(f) *Attestation report on internal control over financial reporting.* (1) Every registered public accounting firm that

issues or prepares an accountant's report for a registrant, other than a registrant that is neither an accelerated filer nor a large accelerated filer (as defined in §240.12b-2 of this chapter) or an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), that is included in an annual report required by section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*) containing an assessment by management of the effectiveness of the registrant's internal control over financial reporting must include an attestation report on internal control over financial reporting.

(2) If an attestation report on internal control over financial reporting is included in an annual report required by section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*), it shall clearly state the opinion of the accountant, either unqualified or adverse, as to whether the registrant maintained, in all material respects, effective internal control over financial reporting, except in the rare circumstance of a scope limitation that cannot be overcome by the registrant or the registered public accounting firm which would result in the accounting firm disclaiming an opinion. The attestation report on internal control over financial reporting shall be dated, signed manually, identify the period covered by the report and indicate that the accountant has audited the effectiveness of internal control over financial reporting. The attestation report on internal control over financial reporting may be separate from the accountant's report.

(g) *Attestation report on assessment of compliance with servicing criteria for asset-backed securities.* The attestation report on assessment of compliance with servicing criteria for asset-backed securities, as required by §240.13a-18(c) or §240.15d-18(c) of this chapter, shall be dated, signed manually, identify the period covered by the report and clearly state the opinion of the registered public accounting firm as to whether the asserting party's assessment of compliance with the servicing criteria is fairly stated in all material respects, or must include an opinion to the effect that an overall opinion cannot be

expressed. If an overall opinion cannot be expressed, explain why.

[37 FR 14594, July 21, 1972, as amended at 41 FR 35479, Aug. 23, 1976; 45 FR 63668, Sept. 25, 1980; 50 FR 25215, June 18, 1985; 67 FR 13533, Mar. 22, 2002; 68 FR 36660, June 18, 2003; 70 FR 1593, Jan. 7, 2005; 72 FR 35321, June 27, 2007; 75 FR 57387, Sept. 21, 2010]

§210.2-03 Examination of financial statements by foreign government auditors.

Notwithstanding any requirements as to examination by independent accountants, the financial statements of any foreign governmental agency may be examined by the regular and customary auditing staff of the respective government if public financial statements of such governmental agency are customarily examined by such auditing staff.

§210.2-04 Examination of financial statements of persons other than the registrant.

If a registrant is required to file financial statements of any other person, such statements need not be examined if examination of such statements would not be required if such person were itself a registrant.

§210.2-05 Examination of financial statements by more than one accountant.

If, with respect to the examination of the financial statements, part of the examination is made by an independent accountant other than the principal accountant and the principal accountant elects to place reliance on the work of the other accountant and makes reference to that effect in his report, the separate report of the other accountant shall be filed. However, notwithstanding the provisions of this section, reports of other accountants which may otherwise be required in filings need not be presented in annual reports to security holders furnished pursuant to the proxy and information statement rules under the Securities Exchange Act of 1934 [§§ 240.14a-3 and 240.14c-3].

[46 FR 40872, Aug. 13, 1981]

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§210.2-06 Retention of audit and review records.

(a) For a period of seven years after an accountant concludes an audit or review of an issuer's financial statements to which section 10A(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(a)) applies, or of the financial statements of any investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), the accountant shall retain records relevant to the audit or review, including workpapers and other documents that form the basis of the audit or review, and memoranda, correspondence, communications, other documents, and records (including electronic records), which:

(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.

(b) For the purposes of paragraph (a) of this section, *workpapers* means documentation of auditing or review procedures applied, evidence obtained, and conclusions reached by the accountant in the audit or review engagement, as required by standards established or adopted by the Commission or by the Public Company Accounting Oversight Board.

(c) Memoranda, correspondence, communications, other documents, and records (including electronic records) described in paragraph (a) of this section shall be retained whether they support the auditor's final conclusions regarding the audit or review, or contain information or data, relating to a significant matter, that is inconsistent with the auditor's final conclusions regarding that matter or the audit or review. Significance of a matter shall be determined based on an objective analysis of the facts and circumstances. Such documents and records include, but are not limited to, those documenting a consultation on or resolution of differences in professional judgment.

(d) For the purposes of paragraph (a) of this section, the term *issuer* means an issuer as defined in section 10A(f) of

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the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f)).

[68 FR 4872, Jan. 30, 2003]

§210.2-07 Communication with audit committees.

(a) Each registered public accounting firm that performs for an audit client that is an issuer (as defined in section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f))), other than an issuer that is an Asset-Backed Issuer as defined in §229.1101 of this chapter, or an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), other than a unit investment trust as defined by section 4(2) of the Investment Company Act of 1940 (15 U.S.C. 80a-4(2)), any audit required under the securities laws shall report, prior to the filing of such audit report with the Commission (or in the case of a registered investment company, annually, and if the annual communication is not within 90 days prior to the filing, provide an update, in the 90 day period prior to the filing, of any changes to the previously reported information), to the audit committee of the issuer or registered investment company:

(1) All critical accounting policies and practices to be used;

(2) All alternative treatments within Generally Accepted Accounting Principles for policies and practices related to material items that have been discussed with management of the issuer or registered investment company, including:

(i) Ramifications of the use of such alternative disclosures and treatments; and

(ii) The treatment preferred by the registered public accounting firm;

(3) Other material written communications between the registered public accounting firm and the management of the issuer or registered investment company, such as any management letter or schedule of unadjusted differences;

(4) If the audit client is an investment company, all non-audit services provided to any entity in an investment company complex, as defined in §210.2-01 (f)(14), that were not pre-approved by the registered investment

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company's audit committee pursuant to § 210.2-01 (c)(7).

(b) [Reserved]

[68 FR 6048, Feb. 5, 2003, as amended at 70 FR 1593, Jan. 7, 2005]

GENERAL INSTRUCTIONS AS TO FINANCIAL STATEMENTS

SOURCE: Sections 210.3-01 through 210.3-16 appear at 45 FR 63687, Sept. 25, 1980, unless otherwise noted.

NOTE: These instructions specify the balance sheets and statements of income and cash flows to be included in disclosure documents prepared in accordance with Regulation S-X. Other portions of Regulation S-X govern the examination, form and content of such financial statements, including the basis of consolidation and the schedules to be filed. The financial statements described below shall be audited unless otherwise indicated.

For filings under the Securities Act of 1933, attention is directed to § 230.411(b) regarding incorporation by reference to financial statements and to section 10(a)(3) of the Act regarding information required in the prospectus.

For filings under the Securities Exchange Act of 1934, attention is directed to § 240.12b-23 regarding incorporation by reference and § 240.12b-36 regarding use of financial statements filed under other acts.

[45 FR 63687, Sept. 25, 1980, as amended at 57 FR 45292, Oct. 1, 1992]

§ 210.3-01 Consolidated balance sheets.

(a) There shall be filed, for the registrant and its subsidiaries consolidated, audited balance sheets as of the end of each of the two most recent fiscal years. If the registrant has been in existence for less than one fiscal year, there shall be filed an audited balance sheet as of a date within 135 days of the date of filing the registration statement.

(b) If the filing, other than a filing on Form 10-K or Form 10, is made within 45 days after the end of the registrant's fiscal year and audited financial statements for the most recent fiscal year are not available, the balance sheets may be as of the end of the two preceding fiscal years and the filing shall include an additional balance sheet as of an interim date at least as current as the end of the registrant's third fiscal quarter of the most recently completed fiscal year.

(c) The instruction in paragraph (b) of this section is also applicable to filings, other than on Form 10-K or Form 10, made after 45 days but within the number of days of the end of the registrant's fiscal year specified in paragraph (i) of this section: *Provided*, that the following conditions are met:

(1) The registrant files annual, quarterly and other reports pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 and all reports due have been filed;

(2) For the most recent fiscal year for which audited financial statements are not yet available the registrant reasonably and in good faith expects to report income attributable to the registrant, after taxes but before extraordinary items and cumulative effect of a change in accounting principle; and

(3) For at least one of the two fiscal years immediately preceding the most recent fiscal year the registrant reported income attributable to the registrant, after taxes but before extraordinary items and cumulative effect of a change in accounting principle.

(d) For filings made after 45 days but within the number of days of the end of the registrant's fiscal year specified in paragraph (i) of this section where the conditions set forth in paragraph (c) of this section are not met, the filing must include the audited balance sheets required by paragraph (a) of this section.

(e) For filings made after the number of days specified in paragraph (i)(2) of this section, the filing shall also include a balance sheet as of an interim date within the following number of days of the date of filing:

(1) 130 days for large accelerated filers and accelerated filers (as defined in § 240.12b-2 of this chapter); and

(2) 135 days for all other registrants.

(f) Any interim balance sheet provided in accordance with the requirements of this section may be unaudited and need not be presented in greater detail than is required by § 210.10-01. Notwithstanding the requirements of this section, the most recent interim balance sheet included in a filing shall be at least as current as the most recent balance sheet filed with the Commission on Form 10-Q.