CAQ Alert 2021-02:

Amendments to SEC Independence Rules

June 2021

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See Final Rule

The Securities and Exchange Commission (SEC) approved amendments to certain auditor independence requirements in Rule 2-01 of Regulation S-X in October 2020. These amendments are effective June 9, 2021. Voluntary early compliance is permitted after December 11, 2020 (the date the amendments were published in the Federal Register) in advance of the effective date provided that the final amendments are applied in their entirety from the date of early compliance.[1]

The final SEC amendments modernize the rules and more effectively focus the independence analysis on relationships and services that may pose threats to an auditor's objectivity and impartiality. The amendments were informed by decades of staff experience applying the auditor independence framework.

This Alert provides an overview of the amendments to assist auditors and other stakeholders with understanding and applying the independence rules and the key changes included in the amendments. This Alert is structured as follows:

Section 1: Auditor Independence Is Fundamental to Audit Quality – What Hasn't Changed

Section 2: Overview of the Amendments – Key Changes

+ Definition of an Affiliate

+ "Look-back" Period

+ Student and Consumer Loans

+ Business Relationship Rule

+ Transition Framework for Mergers & Acquisitions (M&A) Activity

Appendix: Final Rule 2-01 Marked for Changes[2]

SECTION 1: AUDITOR INDEPENDENCE IS FUNDAMENTAL TO AUDIT QUALITY – WHAT HASN'T CHANGED

As required by the Sarbanes-Oxley Act of 2002, the SEC established strict rules that have served as the gold standard of auditor independence for nearly 20 years. The auditing profession is committed to auditor independence, which is foundational to audit quality.

The SEC modernized its 20-year-old auditor independence rules to reflect increasingly complex and interconnected capital markets, including the expansion of investment funds. Investment funds are fundamental to the economic prosperity of many Americans who have retirement accounts.

Importantly, the SEC's changes to the auditor independence rules do not weaken auditor independence. The safeguards protecting auditor independence remain strong. The amendments serve to focus the independence requirements on those relationships and services that are more likely to threaten an auditor's objectivity and impartiality in light of current market conditions and industry practice.

Further, what's called the "general standard" – Rule 2-01(b) – didn't change. This is an overarching rule which serves as a lens through which all services and relationships are viewed. Rule 2-01(b) states:

> *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.*

1 On November 19, 2020, the Public Company Accounting Oversight Board (PCAOB) adopted amendments to its independence standards to align its requirements with the SEC's revisions. On January 14, 2021, the SEC approved the PCAOB's amendments.

2 The Appendix is a work product of the CAQ for informational purposes and was not produced by the SEC.

To determine whether an auditor is independent under this standard all of the relationships between the auditor and the company, the company's management and directors, need to be considered; not just those relationships related to reports filed with the Commission. The following guiding principles should be considered as to whether a relationship with or service provided by an auditor:

(a) creates a mutual or conflicting interest with their audit client;

(b) places them in the position of auditing their own work;

(c) results in their acting as management or an employee of the audit client; or

(d) places them in a position of being an advocate for the audit client.[3]

Therefore, even in circumstances when a service or relationship is not explicitly prohibited by the independence rules under Rule 2-01, the general standard requires auditors, audit committee members, and management to evaluate a service or relationship from the perspective of a reasonable investor and determine whether there is a real or perceived impact on the auditor's objectivity and impartiality.[4]

SECTION 2: OVERVIEW OF THE AMENDMENTS – KEY CHANGES

The key changes the SEC made to Rule 2-01:[5]

+ Amend the definitions of "affiliate of the audit client," in Rule 2-01(f)(4), and "investment company complex," in Rule 2-01(f)(14), to address certain affiliate relationships, including entities under common control;

+ Amend the definition of "audit and professional engagement period," specifically Rule 2-01(f)(5)(iii), to shorten the "look-back" period for domestic first-time filers in assessing compliance with the independence requirements;

+ Amend Rule 2-01(c)(1)(ii)(A)(1) and (E) to add certain student loans and de minimis consumer loans to the categorical exclusions from independence-impairing lending relationships;

+ Amend Rule 2-01(c)(3) to replace the reference to "substantial stockholders" in the business relationships rule with the concept of beneficial owners with significant influence over the entity under audit;

+ Add a new provision to Rule 2-01(e) to introduce a transition framework to address inadvertent independence violations that only arise as a result of a merger or acquisition transaction; and

+ Make certain other miscellaneous updates.

Let's break down these changes into plain English.

Definition of an Affiliate

+ "Audit client" is defined as the entity whose financial statements or other information is being audited, reviewed, or attested to *and any affiliates of the audit client*.[6]

+ The entity whose financial statements or other information is being audited, reviewed, or attested is the "entity under audit." Auditors must be independent of their "audit client" which includes the "entity under audit" and its "affiliates."

+ What is an affiliate? Affiliates refer to certain entities *related to* the entity under audit and always include an entity or entities that have control over the entity

3 See SEC website, https://www.sec.gov/info/accountants/audit042707.htm.

4 See page 31 of the Release, which states: "…we are clarifying that the types of relationships and services that must be evaluated under Rule 2-01(b) are those that are known or should be known to the auditor because of the nature, extent, relative importance or other relevant aspects of the relationships or services."

5 Derived from SEC press release, *SEC Updates Auditor Independence Rule* (October 16, 2020).

6 As defined by Rule 2-01(f)(6). The full definition is, "***Audit client*** means the entity whose financial statements or other information is being audited, reviewed, or attested to 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)(iii), (f)(4)(iv), or (f)(14)(i)(E) of this section.

under audit (e.g., parent companies, funds) or over which the entity under audit exercises control (e.g., subsidiaries, portfolio companies).

+ Prior to the amendments, entities under common control with the entity under audit (sister entities) were always affiliates, including sister entities that are part of an investment company complex (ICC).[7]

+ Over time, the number of affiliates has grown to hundreds or thousands of entities for some companies – especially in the private equity space. Some affiliates may have strong, material relationships that significantly impact a company's business, but other affiliates, particularly sister entities, often have only insignificant tangential relationships that do not impact a company's business.

+ The amendments clarify that "affiliates of the audit client" definition should be applied to an operating company[8] under audit, and the amended ICC definition should be applied to each entity under audit that is an investment company or an investment adviser or sponsor.

+ For sister entities of operating companies, the SEC introduced a dual materiality threshold to determine whether the entity is an affiliate. Under the amendments, if either the entity under audit or the sister entity is not material to the controlling entity, the sister entity is not an affiliate of the entity under audit. If the information is not available to make reasonable materiality determinations, generally, the sister entity should be treated as an affiliate. This change better focuses the independence analysis on relationships with the entity under audit that are relevant to the auditor's objectivity and impartiality.

+ The auditor's non-audit services to and relationships with sister entities that are no longer deemed affiliates as a result of applying the dual materiality threshold will continue to be subject to the principles set forth in Rule 2-01(b), and as such, knowledge of services to and relationships with such non-affiliate sister entities will be needed to sufficiently evaluate compliance with the general standard.[9]

+ The amended ICC definition in Rule 2-01(f)(14):[10]

  - Requires use of the term "entity under audit" as the starting point for an analysis of entities included in the ICC.

  - Clarifies that the definition of an ICC includes unregistered funds.

  - Contains a significant influence provision that pulls the following entities into the ICC definition when the entity under audit is an investment company or an investment advisor/sponsor:

    - when the entity under audit has significant influence over an entity and the entity is material to the entity under audit.

    - when an entity has significant influence over the entity under audit and the entity under audit is material to the entity.

  - Includes in the definition any sister investment advisers or sponsors where a dual material relationship exists.

  - Includes in the definition a sister investment company that shares the same adviser or sponsor as an investment company under audit, regardless of whether such entity is material to the shared investment adviser or sponsor.

  - Applies a dual materiality threshold for portfolio companies of sister investment companies that are controlled by the same investment adviser or sponsor, unless the portfolio companies are engaged in the business of providing administrative, custodial, underwriting, or transfer agent services.

7 As defined by Rule 2-01(f)(14).

8 See page 8, FN 22 of the Release which states, "The term "operating company" in this release refers to entities that are not investment companies, investment advisers, or sponsors."

9 See page 17 of the Release.

10 Derived from *SEC amends certain auditor independence requirements*, Grant Thornton (November 4, 2020).

Example A

- An audit firm is considering providing a payroll service to an Australian lodging company (Company A). Company A is controlled by Fund A. Company A is not material to Fund A. The audit firm does not audit Company A or Fund A. The audit firm audits a separate U.S. electronics manufacturer (Company B) that is controlled by and material to Fund A. There is no relationship between the companies A and B other than the fact that they are controlled by Fund A. Given that Company A is not material to Fund A, Company A is not an affiliate of Company B.

- In the example above, although Company A is not an affiliate of Company B, the auditor of Company B would still need to comply with the general standard of auditor independence as it applies to services or relationships that are known or should be known to the auditor due to its nature, extent, relative importance, or other relevant aspects of the service or relationship.[11]

"Look-back" Period

- Under the independence rules established nearly two decades ago, domestic public company auditors were required to comply with SEC independence requirements for all historical financial statement periods included in an initial public offering (IPO) registration statement, which is generally two or three years.

- This extended "look-back" period at times could result in challenges, cost or delays to an IPO, typically without identifying situations that impacted auditor objectivity and impartiality.[12]

- The SEC shortened the "look-back" period to one year for domestic first-time filers, which aligns the requirements with those of foreign private issuers.[13] The amended "look-back" period also applies to a private company merging with a Special Purpose Acquisition Companies (SPAC) in a de-SPAC transaction.[14]

- For all periods included in a filing, the auditors must comply with applicable independence standards. Relationships and services in prior years included in a filing that would not be in the "look-back" period must still be considered under the SEC general independence standard of Rule 2-01(b), either individually or in the aggregate.[15]

- The amendments provide some flexibility for private companies intending to go public, although such intent continues to require advance planning and consideration of time needed for auditors to comply with PCAOB standards and SEC rules.

Example B

- BOOM, a U.S. based video conference company, files an IPO registration statement with the SEC on April 15, 20x5. This registration statement includes audited financial statements for the past three years – 20x2-20x4 when BOOM was a private company.[16] BOOM is audited by an auditor who complied as required with the AICPA auditor independence standards during these periods. When BOOM commenced operations, they weren't sure when or if they would go public, and therefore engaged its auditor to conduct audits under AICPA standards (i.e., US generally accepted auditing standards).

- Under the SEC independence rules prior to the amendments, BOOM's auditor would have had to comply with the SEC independence rules for all financial statement periods in the registration statement (20x2-20x4). Under the amended rules,

11 See page 31 of the Release for additional discussion by the staff.

12 See page 50 of the Release which cites the views of certain commenters.

13 See the amended definition of the audit and professional engagement period in Rule 2-01(f)(5)(iii).

14 See CAQ Alert 2021-01: *Auditor and Audit Committee Considerations Relating to Special Purpose Acquisitions Company (SPAC) Initial Public Offerings and Mergers* (May 2021) for more information about SPACs.

15 See page 49 of the Release.

16 For purposes of illustration, it is assumed that all periods included in the registration statement are subsequent to the effective date of the independence rule amendments.

BOOM's auditor would need to comply with SEC independence rules only for the 20x4 audit if it complied with AICPA independence standards for the 20x2 and 20x3 audits. However, as previously noted, the auditor must comply with the SEC general standard, including consideration of the four independence principles, for all periods included in the filing.

Student and Consumer Loans

+ The amended rules permit covered persons[17] to have certain student loans and small consumer loans (e.g., retail installment loan, cell phone installment plans, and home improvement loans that are not secured by a mortgage on a primary residence) with audit clients and their affiliates.

+ Under the independence rules prior to the amendments, for example, a public company audit firm could not audit a bank without triggering an independence violation if a covered person had a student loan at that bank, even if the loan was obtained prior to the covered person's employment with the firm. The amended rules permit student loans provided the loans were not obtained while the professional was a covered person.

+ The amendments replaced the reference to "credit cards" with "consumer loans" in Rule 2-01(c)(1)(ii)(E). The amendments permit any consumer loan with a lender that is an audit client as long as the aggregate outstanding balance owed is reduced to $10,000 or less on a current basis taking into consideration the payment due date and available grace period. This represents the Commission's view that a limited amount of debt that is routinely incurred by a covered person or any of his or her immediate family members for personal consumption, even if the audit client is the lending entity, would typically not impair an auditor's objectivity and impartiality.[18]

Example C

+ Shannon, an audit partner based in the Delaware office of Audit Firm LLP, took out student loans to attend The Ohio State University prior to starting her career. Shannon continues to pay her student loans to Student Loan Lender. Ashley, a different audit partner in the Delaware office, is the lead audit partner assigned to Audit Firm LLP's audit of Student Loan Lender. Accordingly, Shannon is considered a covered person on the audit of Student Loan Lender because she is a partner in the same office as Ashley.

+ Under the independence rules prior to the amendments, Shannon's student loan would lead to an independence violation for the audit engagement of Student Loan Lender. Under the amended rules, Shannon's student loan would no longer result in an independence violation for the audit engagement of the lender because it was obtained before she became a covered person.

Business Relationships Rule

+ The Business Relationships Rule (BRR) prohibits auditors from having a business relationship with their audit clients unless the transaction relates to the audit firm providing professional services or the audit firm is a consumer in the ordinary course of business. Can the auditor create a joint venture with an audit client to sell audit software? No. Can the auditor buy paper from OfficeSupply Co. in the ordinary course of business even if they audit OfficeSupply Co.? Generally, yes. The amendments do not fundamentally change this principle.

17 Covered persons in the firm is defined in Rule 2-01(f)(11) to mean the following partners, principals, shareholders, and employees of an accounting firm:
(i) The "audit engagement team" [as defined by Rule 2-01(f)(7)(i)];
(ii) The "chain of command" [as defined by Rule 2-01(f)(8)];
(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.

18 See page 59 of the Release.

- The BRR also prohibits auditors from having a business relationship with persons[19] who can influence the entity under audit – including officers and directors and, prior to the amendments, "substantial stockholders."

- The term "substantial stockholder" was replaced with the concept of beneficial owner with "significant influence over the entity under audit." This change in terminology clarified the rule. The amendment now restricts business relationships with persons who are beneficial owners of (e.g., have an economic interest in) the audit client's equity securities where such beneficial ownership has significant influence over the entity under audit.

- Under the independence rules prior to the amendments, the audit firm of the public company was not permitted to have a business relationship with any "substantial stockholder" of an audit client. The term "substantial stockholder" was undefined.

- The amendments align the stockholders restricted by the BRR to those beneficial owners with significant influence over the entity under audit. This allows auditors to apply a significant influence concept that is widely understood due to its connection to the accounting standards and other provisions of the SEC independence rules (e.g., the affiliate and ICC definitions and the Loan Provision).[20]

- Under the amended rules, the audit firm of the public company cannot have a prohibited business relationship with the beneficial owner that has significant influence over the entity under audit.

Example D

- An audit firm audits a public paper company. For simplicity, this example assumes no affiliates.

- David Smith is a substantial stockholder but not a beneficial owner with significant influence over the paper company.

- Under the pre-amendment rule, the audit firm could not have a business relationship with David Smith, the substantial stockholder in the paper company. Under the amendments, the audit firm is permitted to have a business relationship with David Smith because he does not have significant influence over the audit client.

Transition Framework for M&A Activity

- When a public company merger or acquisition occurs, the auditor of the acquiring company is required to be independent of the acquired company. This requirement has not changed.

- The amendments include a new transition provision for M&A transactions that would otherwise cause inadvertent independence violations.

- When relationships or services that are not permissible under the SEC independence rules arise as a result of M&A transactions and are identified prior to the effective date of the transaction but cannot be resolved before the effective date of the transaction without significant disruption to the audit client, the firm's independence is not impaired assuming corrective measures are taken promptly post-closing, and a system of quality control is maintained by the auditor.

- In addition, continuing the otherwise impermissible service or relationship after the effective date of the transaction must be consistent with the SEC's general standard of auditor independence. That is, a reasonable investor would conclude that the auditor remains capable of exercising objective and impartial judgment.

- Before the amendments, a merger or acquisition resulting in an independence violation was not provided any transition period for resolution, even if there was no effect on the objectivity and impartiality of the auditor.

19 In this context and throughout this section, persons include both individuals and entities.

20 See *Auditor Independence With Respect to Certain Loans or Debtor-Creditor Relationships*, Release 33- 10648 (June 18, 2019) [84 FR 32040 (July 5, 2019)]. In this release, references to the "Loan Provision" mean 17 CFR 210.2-01(c)(1)(ii)(A).

- When an audit client is planning an acquisition, all the relationships with and services provided to the acquired entity must be assessed prior to the effective date of the transaction to determine if the auditor is independent. The SEC's amended independence rules recognize that auditors are expected to resolve potential inadvertent independence issues in advance of the merger except where the transition would cause a significant disruption to the audit client.

- The auditor is required to address any inadvertent non-compliance with the independence rules noted above in a prompt manner. The rules do not provide a specified time period. The SEC has indicated they consider no later than six months to be reasonable, but they also indicated a shorter period should be used when reasonably attainable and more appropriate.[21]

- If an impermissible service or relationship is identified after the transaction effective date, that service or relationship will result in an independence violation, and the transition provision does not apply to that service or relationship.[22]

Example E

- A large public sporting goods company (SGC) acquires a small rubber manufacturer outside the United States. The auditor of SGC provides payroll services to the rubber manufacturer. The information about the acquisition and the impermissible payroll services was identified by the audit client's and audit firm's processes before the effective date of the acquisition but there is not enough time for the auditor to extract itself from providing the service by the effective date without causing significant disruption to the rubber manufacturer. The rubber manufacturer has few employees, and the payroll expenditures of the rubber company are immaterial to SGC.

- Under the independence rules prior to the amendments, the auditor of SGC violated the independence rules if the payroll services were provided to the rubber manufacturer after the effective date of the acquisition. This is regardless of whether the auditor and the audit committee determined that: (1) the auditor's objectivity and impartiality would not be impaired, (2) the service is terminated shortly after the effective date of the acquisition when a new service provider is identified, and (3) the services are promptly transitioned.

- Under the amended rules, the auditor is still required to stop providing the payroll service to the newly acquired rubber company as soon as possible but providing such services after the effective date of the transaction would not impair the auditor's independence.

Maintaining auditor independence is a shared responsibility. Accounting firms are required to have in place procedures and controls – working jointly with their audit clients – that monitor the audit client's merger and acquisition activity to provide timely notice of a merger or acquisition and allow for the identification of impermissible services and relationships before the effective date of a merger or acquisition. The transition provisions are not intended to provide a free pass. Under the amended rules, it is still expected that all prohibited relationships and services be addressed before the merger/acquisition effective date to the extent possible, without causing significant disruption to the audit client. The transition provision acknowledges that facts and circumstances arise in

21 See page 77 of the Release which states, "We expect any necessary actions would be taken no later than six months after the effective date of the merger or acquisition. We have not included a reference to the six-month maximum transition period in amended Rule 2-01(e), as suggested by some commenters, because we do not intend, nor do we believe it would be appropriate, for audit clients and audit firms to apply this timeline to address such services or relationships in every merger or acquisition scenario. In this regard, we agree with the commenter who suggested that specifying such a timeline in the final rule could result in it becoming the standard practice in all situations, even when a shorter transition may be reasonably attainable and more appropriate."

22 See pages 78-79 of the Release which states, "In situations where a service or relationship resulting in an independence violation is identified subsequent to the effective date of the transaction, an audit firm and the audit client's audit committee will need to take into account all relevant facts and circumstances in their evaluation of the auditor's objectivity and impartiality in carrying out an audit of the financial statements of the combined entity."

which a service or relationship cannot be resolved prior to the effective date without causing significant disruption, and provide a transition period to resolve the situation.

CONCLUSION

Auditor independence is foundational to audit quality. The targeted amendments to the independence rules adopted by the SEC are intended to modernize and improve the application of the rules in practice. Compliance with these rules is a shared responsibility among management, auditors, and audit committees, and requires timely, accurate information to complete an informed analysis.

Appendix

Final Rule 2-01 Marked for Changes

Notations about this Appendix:

- The Appendix is a work product of the CAQ for informational purposes and was not produced by the SEC.
- Gray text is used to indicate there is no change to the paragraph as a result of the final amendments approved by the SEC in October 2020.
- Red text reflects the changes due to the final amendments.

Introductory Text / Rule 2-01(a)

§ 210.2-01 Qualifications of accountants.

The following text was previously a Preliminary Note to Rule 2-01 and was converted into introductory text:

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.

Section 210.2-01(b) sets forth the general standard of auditor independence. Paragraphs (c)(1) to (c)(5) of this section 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.

These factors are general guidance only, and their application may depend on particular facts and circumstances. For that reason, §210.2- 01(b) 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.

2-01(a)

(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.

Rule 2-01(b)

2-01(b)

(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.

Rule 2-01(c)

2-01(c)

(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.***

(1) Any loan (including any margin loan) to or from an audit client, ~~or~~ an audit client's officers or; directors that have the ability to affect decision-making at the entity under audit, or beneficial owners (known through reasonable inquiry) of the audit client's equity securities where such beneficial owner has significant influence over the entity under audit ~~client~~. The following loans obtained from a financial institution under its normal lending procedures, terms, and requirements are excepted from this paragraph (c)(1)(ii)(A)(1)~~, except for the following loans obtained from a financial institution under its normal lending procedures, terms, and requirements~~:

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

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

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

(iv) ~~A m~~Mortgage loans collateralized by the borrower's primary residence provided the loans ~~was~~ were not obtained while the covered person in the firm was a covered person; and

(v) *Student loans provided the loans were not obtained while the covered person in the firm was a covered person~~.~~*

(2) For purposes of paragraph (c)(1)(ii)(A) of this section:

(i) The term *audit client* for a fund under audit excludes any other fund that otherwise would be considered an *affiliate of the audit client;*

(ii) The term *fund* means: An investment company or an 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)); or a commodity pool as defined in Section 1a(10) of the U.S. Commodity Exchange Act, as amended [(7 U.S.C. 1-1a(10)], that is not an investment company or an 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)).

(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

(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***~~***Consumer loans.*** Any aggregate outstanding ~~credit card~~consumer loan 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 following individuals are not considered to be members of the audit engagement team:

(i) Persons, other than the lead partner and the ~~concurring partner~~ Engagement Quality Reviewer, who provided 10~~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~~the Engagement Quality Reviewer, who provided 10~~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 or~~,~~ directors that have the ability to affect decision-making at the entity under audit or beneficial owners (known through reasonable inquiry) of the audit client's equity securities where such beneficial owner has significant influence over the entity under audit~~, or substantial stockholders~~. The relationships described in this paragraph (c)(3) 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~~ Engagement Quality Reviewer, 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~~Engagement Quality Reviewer, 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 investment 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.

Rule 2-01(d)

2-01(d)

(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. 78*l*), 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.

Rule 2-01(e)

2-01(e)

(e) ***Transition provisions for mergers and acquisitions involving audit clients.*** An accounting firm's independence will not be impaired because an audit client engages in a merger or acquisition that gives rise to a relationship or service that is inconsistent with this rule, provided that:

(1) The accounting firm is in compliance with the applicable independence standards related to such services or relationships when the services or relationships originated and throughout the period in which the applicable independence standards apply; ~~***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) The accounting firm has or will address such services or relationships promptly under relevant circumstances as a result of the occurrence of the merger or acquisition;~~***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.~~

(3) The accounting firm has in place a quality control system as described in paragraph (d)(3) of this section that has the following features:

(i) Procedures and controls that monitor the audit client's merger and acquisition activity to provide timely notice of a merger or acquisition; and

(ii) Procedures and controls that allow for prompt identification of such services or relationships after initial notification of a potential merger or acquisition that may trigger independence violations, but before the effective date of the transaction.

Rule 2-01(f)

2-01(f)

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

(ii) An entity that is under common control with the entity under audit, including the entity under audit's parents and subsidiaries, when the entity and the entity under audit are each material to the controlling entity;

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

(i~~v~~vii) An entity that has significant influence over the audit client, unless the audit client is not material to the entity; ~~and~~or

(~~i~~iv) Each entity in the investment company complex as determined in paragraph (f)(14) of this section when the entity under audit ~~client~~ is an ~~entity that is part of an~~ investment company ~~complex~~or investment adviser or sponsor, as those terms are defined in paragraphs (f)(14)(ii), (iii), and (iv) of this section.

(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, t~~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~~applicable 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 to 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 paragraphs (f)(4)(iii), (f)(4)(iv), or (f)(14)(~~ii~~)(E) 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 conducting a quality review under applicable professional standards and any applicable rules of the Commission to evaluate the significant judgments and the related conclusions reached in forming the overall conclusion on the audit or review engagement ("Engagement Quality Reviewer" or "Engagement Quality Control Reviewer");

(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 entity under audit that is an:

(1) ~~i~~investment company; or

(2) ~~and its i~~Investment adviser or sponsor;

(B) ~~Any entity controlled by or controlling an~~The investment adviser or sponsor of any investment company identified in paragraph (f)(14)(i)(A)*(1)* of this section~~,~~;

(C) ~~or a~~Any entity controlled by or controlling:

(1)~~under common control with an investment adviser or sponsor~~An entity under audit identified by paragraph (f)(14)(i)(A) of this section, or ~~if the entity:~~

~~*(1)* Is an investment adviser or sponsor; or~~*(2)* An investment adviser or sponsor identified by paragraph (f)(14)(i)(B) of this section. When the entity is controlled by an investment adviser or sponsor identified by paragraph (f)(14)(i)(B), such entity is included within the investment company complex if:

(i) The entity and the entity under audit are each material to the investment adviser or sponsor identified by paragraph (f)(14)(i)(B) of this section; or

(ii) The entity ~~is~~ is engaged in the business of providing administrative, custodial, underwriting, or transfer agent services to any ~~investment company, investment adviser, or sponsor; and~~entity identified by paragraphs (f)(14)(i)(A) or (B) of this section;

(D) Any entity under common control with an entity under audit identified by paragraph (f)(14)(i)(A) of this section, any investment adviser or sponsor identified by paragraph (f)(14)(i)(B) of this section, or any entity identified by paragraph (f)(14)(i)(C) of this section; if the entity:

(1) Is an investment company or an investment adviser or sponsor, when the entity and the entity under audit identified by paragraph (f)(14)(i)(A) of this section are each material to the controlling entity; or

(2) Is engaged in the business of providing administrative, custodian, underwriting, or transfer agent services to any entity identified by paragraphs (f)(14)(i)(A) and (f)(14)(i)(B) of this section;

(E) Any entity over which an entity under audit identified by paragraph (f)(14)(i)(A) of this section has significant influence, unless the entity is not material to the entity under audit identified by paragraph (f)(14)(i)(A) of this section, or any entity that has significant influence over an entity under audit identified by paragraph (f)(14)(i)(A) of this section, unless the entity under audit identified by paragraph (f)(14)(i)(A) of this section is not material to the entity that has significant influence over it; and

(F) Any investment company that has an investment adviser or sponsor included in this definition by paragraphs (f)(14)(i)(A) through (f)(14)(i)(D) of this section.

(ii)~~**(C)**~~ An investment company, for purposes of paragraph (f)(14) of this section, means ~~A~~any investment company or an 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~~.

(iii) 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.

(iv~~**ii**~~**)** 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)).