

MEMO# 15398

November 26, 2002

SEC PROPOSAL ON AUDITOR RECORD RETENTION

[15398] November 26, 2002 TO: ACCOUNTING/TREASURERS COMMITTEE No. 52-02 CLOSED-END INVESTMENT COMPANY COMMITTEE No. 47-02 INVESTMENT ADVISERS COMMITTEE No. 28-02 SEC RULES COMMITTEE No. 96-02 SMALL FUNDS COMMITTEE No. 20-02 UNIT INVESTMENT TRUST COMMITTEE No. 26-02 RE: SEC PROPOSAL ON AUDITOR RECORD RETENTION The SEC has issued a release proposing a rule that would require accounting firms to retain for five years certain records relevant to their audits and reviews of issuers' financial statements.¹ Proposed Rule 2-06 of Regulation S-X is intended to implement Section 802 of the Sarbanes-Oxley Act of 2002. While this proposed rule relates primarily to auditor record retention, there are several issues of interest to investment companies, described more fully below. Comments on the proposal are due by Friday, December 27, 2002. We plan to hold a conference call on the proposal shortly and will inform you of the date and time via email as soon as possible. Proposed Rule The Commission has proposed to amend Regulation S-X to require accountants who audit or review an issuer's financial statements to retain certain records relevant to that audit or review for a period of five years from the end of the fiscal year in which an audit or review was concluded.² Auditors would be required to retain workpapers and other documents that form the basis of the audit or review of an issuer's financial statements, and memoranda, correspondence, communications, other documents, and records (including electronic records) that meet two criteria. The two criteria are that the materials (1) are created, sent or received in connection with the audit or review, and (2) contain conclusions, opinions, analyses, or financial data related to the audit or review. 1 SEC Release No. 33-8151, 34-46869, IC-25830 (November 21, 2002) ("Release"). The Release is available from the SEC's website at <http://www.sec.gov/rules/proposed/33-8151.htm>. 2 The proposed rule applies to the audit of any investment company registered under Section 8 of the Investment Company Act of 1940. 2 The proposed rule is intended to require retention of more than what traditionally has been thought of as an auditor's workpapers. Paragraph (c) of the proposed rule indicates that records to be retained include not only those materials that support an auditor's conclusions about the financial statements but also those that may cast doubt on those conclusions. The Release indicates that paragraph (c) is intended to ensure the preservation of those records that reflect differing professional judgments and views (both within the accounting firm and between the accounting firm and the issuer) and how those differences were resolved. Investment Company Issues The Release notes that Section 32(c) of the Investment Company Act authorizes the Commission to adopt rules to require accountants and auditors to keep reports, work sheets, and other documents and papers relating to registered investment companies for such periods as the Commission may prescribe, and to make these documents and papers available for inspection by the Commission and its staff. The Release requests comment on

whether the Commission should use this authority to extend proposed Rule 2-06 to require that audit workpapers and other documents required to be retained in connection with the audit of investment company financial statements be made available for inspection by the Commission and its staff. The Release notes that audits of many investment advisers and broker-dealers would not be subject to the proposed rule because they are not “issuers” of securities. The Release requests comment on whether the proposal should be amended to apply the record retention requirements to audits of these entities. Finally, the Release requests comment on whether there should be a record retention requirement for issuers as well as auditors. For example, should issuers be required to retain records that the auditor reviewed but did not include in the audit workpapers? Should issuers be required to keep copies of all correspondence with auditors and copies of documents provided to the auditors? Gregory M. Smith Director - Operations/Compliance & Fund Accounting

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