

SEC Proposes Updates to Auditor Independence Requirements

January 7, 2020

On December 30, 2019, the U.S. Securities and Exchange Commission proposed amendments to its auditor independence framework intended to, among other things, reduce the impact the independence rules have on auditor choice, especially in the private equity/asset management industry. Importantly, key aspects of the proposed amendments are intended to address the rigidity inherent in the application of the “common control” element of the auditor independence requirements.

Most significantly, the proposed amendments (the full text of which can be found [here](#)) would, if adopted:

- 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), by, among other things, adding materiality qualifiers and distinguishing how the affiliate definition applies when an accountant is auditing a portfolio company, an investment company or an investment adviser or sponsor;
- shorten the look-back period for domestic first-time filers in assessing compliance with the auditor independence requirements from three years to one year by amending the definition of “audit and professional engagement period,” such that a first-time filer, whether a domestic issuer or a foreign private issuer, would apply Rule 2-01 beginning with the most recently completed fiscal year;
- amend Rule 2-01(c)(1)(ii)(A)(1) and (E) to add certain student loans and *de minimis* consumer loans (defined as having a balance of \$10,000 or less) 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 relationship rule with the concept of beneficial owners with significant influence; and
- replace the outdated transition and grandfathering provision in Rule 2-01(e) with a new Rule 2-01(e) to introduce a transition framework to address inadvertent

independence violations that only arise as a result of merger and acquisition transactions, including that the auditor correct the independence violations as promptly as possible and maintain a quality control system.

The public comment period will remain open for 60 days following publication of the proposing release in the Federal Register.



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