EXECUTIVE INSIGHT

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Corporate Reform

The New SEC Auditor Independence Rules: Implications for Audit Committees and Management

To Our Clients and Other Friends

Faith in the U.S. capital markets has been shaken by high-profile financial frauds, business failures, and corporate governance breakdowns. Restoring the trust and confidence of investors in the capital markets is a responsibility we all share. It's going to take sustained high-quality, high-integrity performance by the accounting profession, corporate management, audit committees and boards of directors, investment bankers, and lawyers. Recognizing that there are no silver bullets or quick fixes, Ernst & Young is committed to doing whatever we can and to providing the highest quality service to help restore investor confidence.

A key element in restoring investor confidence is resolving concerns about auditor independence. The Securities and Exchange Commission (SEC) recently issued its final rules on *Strengthening Auditor Independence* that implement Title II of the Sarbanes-Oxley Act of 2002 (the Act). This is a major step toward bringing finality and clarity to the issue of auditor independence.

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We believe that generally the SEC's final rules strike the right balance in achieving the Act's far-reaching new requirements. These rules, which in many respects exceed the Act's requirements, set forth revised requirements in several areas, including non-audit services, disclosure of fees paid to auditors, audit committee pre-approval of services, audit partner rotation, communications with audit committees, employment of former members of the audit team, and audit partner compensation. In this publication, we summarize the key provisions of the rules.

A focal point of the new auditor independence rules is the importance of the oversight role provided by audit committees. As the SEC notes, "The final rules recognize the critical role played by audit committees in the financial reporting process and the unique position of audit committees in assuring auditor independence." This publication summarizes the implications of these new rules for audit committees, and suggests actions that audit committees should consider in working with management and the independent auditors to implement the new requirements. We have developed an audit committee pre-approval process memorandum and worked with a team of leading securities lawyers at an outside law firm to develop a model pre-approval policy, both of which are included in an appendix to this document. This new direct relationship between independent auditors and audit committees will improve financial reporting. The best results will be achieved when management, the audit committee, and the independent auditors all work closely together while fulfilling their unique roles in the financial reporting process.

We look forward to working closely with you and will be pleased to answer any questions regarding these auditor independence rules or any other matters.

Ernst & Young

Table of Contents

Background on Auditor Independence

Auditor independence has received considerable attention in recent years. In the late 1990s, SEC officials expressed concern about the growth in non-audit services being provided to audit clients. Ernst & Young also became concerned that large-scale, big-fee information technology consulting was increasingly incompatible with the practice of public accounting, and in May 2000 we sold our consulting practice, becoming the first major accounting firm to do so.

When the SEC proposed new independence rules later in 2000, we actively supported the rulemaking initiative. Although those rules did not go as far as we had urged in prohibiting accounting firms from selling information technology consulting services, they did make a number of important improvements to the then-existing independence restrictions.

The scope-of-services debate reemerged last year in the wake of the financial reporting scandals and corporate malfeasance, which contributed to the decline in investor confidence in the U.S. capital markets. Congress, in the Sarbanes-Oxley Act, legislated new auditor independence restrictions and required the SEC to adopt new implementing rules no later than January 26, 2003.

"Congress, after considerable debate and many hearings on the matter, took a clear position aimed at striking the right balance to protect both auditor independence and audit quality."

During the debate, some persons urged Congress to enact a complete ban on non-audit work by the auditing firm. On the other hand, some legislative proposals would have taken no position and left the scope-of-services matter to the SEC and a new accounting regulatory board. Congress, after considerable debate and many hearings on the matter, took a clear position aimed at striking the right balance to protect both auditor independence and audit quality. Starting with a list of services drawn up by the SEC in 2000, Congress drew a "clear line" around its own list of prohibited services. Congress specifically authorized the performance of all non-audit services not on the list, including tax services, while enacting safeguards to enhance auditor independence. Those safeguards include (1) pre-approval by the audit committee of audit and non-audit services, and (2) disclosure to investors of the company's pre-approval policies and its audit and non-audit service fees.

The SEC, in its rulemaking process on *Strengthening Auditor Independence*, was also very deliberate in its evaluation of opinions of all parties. When they reached their decision, the five SEC commissioners voted unanimously to approve the final rule. The unanimous vote sends a very important and clear message to audit committees, investors, and auditors: the issue of independence and non-audit services was extensively reviewed, it was openly debated, and it was decided. Now, audit committees can proceed to adopt the appropriate policies and procedures that support their decision-making process in instances when they choose to obtain non-audit services from their auditing firm.

These new rules will become effective on May 6, 2003, with transition provisions for certain requirements.

Scope of Services Provided by the Auditor

The SEC's final rule on prohibited services adopts the list set forth in Section 201 of the Act. As required by the Act, the rule imposes these three significant new restrictions on non-audit services:

- A prohibition on financial information systems design and implementation services
- A prohibition on internal audit outsourcing services
- A restriction on certain types of "expert" services

All of the SEC's prohibited non-audit services are summarized in the following table.

The Prohibited Non-Audit Services Under the SEC's New Rules	
Bookkeeping	The rule prohibits maintaining or preparing the audit client's accounting records, and preparing the client's financial statements or the source data underlying the financial statements. Although not a significant change from the 2000 rules, the new rule does eliminate exceptions for foreign bookkeeping and temporary and emergency situations.
Financial Information Systems Design and Implementation	The rule prohibits operating or supervising the operation of an audit client's information system or managing the audit client's local area network. It also prohibits 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. (Ernst & Young sold this practice area to the consulting firm of Cap Gemini S.A. in May 2000.) The SEC's rule release clarifies that the rule is not intended to preclude the accountant from making recommendations on internal control matters to management or other service providers in conjunction with the design and installation of a system by another service provider.
Appraisal or Valuation, Fairness Opinion, or Contribution-in-Kind Reports	The rule generally prohibits these services, although the SEC continues to permit valuations for non-financial reporting purposes, including transfer-pricing studies, cost segregation studies, and other tax-only valuations. The SEC's rule release notes that some commentators believed that a strict application of these rules related to contribution-in-kind reports might create conflicts in certain foreign jurisdictions where such reports must be prepared by the company's auditors. The SEC indicated that it is sensitive to these issues and that it will work with other regulatory agencies to resolve them. As under the 2000 rules, we do not believe that there is an independence concern where a contribution-in-kind report is issued as a result of an internal reorganization (typically as a result of a reorganization to achieve tax efficiencies) involving transfers solely among wholly owned subsidiaries (i.e., where there is no effect on an outside minority interest or where there is no outside interest).

The Prohibited Non-Audit Services Under the SEC's New Rules (continued)	
Actuarial Services	The rule prohibits services involving the determination of amounts recorded in the financial statements and related accounts. The rule eliminates the provision in the 2000 rules that allowed accountants to perform actuarial valuations for pension, other post-employment benefits, or similar liabilities. The rule permits assisting a client in understanding the methods, models, assumptions, and inputs used in computing an amount. Also, although not explicitly stated, consistent with the rule on appraisal or valuation services, actuarial services for non-financial reporting purposes, including actuarial work solely for tax purposes, are not prohibited by the rule.
Internal Audit Outsourcing	The rule prohibits any internal audit service that has been outsourced by an audit client that relates to the audit client's internal accounting controls, financial systems, or financial statements. The 2000 rules allowed such services for up to 40% of the total internal audit activities (measured in hours). (In early 2002, Ernst & Young voluntarily decided to stop accepting new internal audit outsourcing engagements for public company audit clients.) The rule does allow operational auditing and non-recurring evaluations of discrete items or other programs, provided they are not in substance outsourcing.
Management Functions	The rule prohibits 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. This basic rule regarding management functions does not represent any significant change from the 2000 rules. The 2000 rules did explicitly permit services in connection with design and implementation of internal accounting controls and risk management controls. The current rule release, however, clarifies that the auditor may not take responsibility for the design and/or implementation of internal accounting or risk management controls. The release indicates the "design and implementation of these controls involves decision-making and, therefore, is different from recommending improvements" in such controls. The rule release makes clear, however, that engagements to make recommendations regarding improvements in internal accounting and risk management controls are permissible.
Human Resources	Although titled "Human Resources," the rule solely prohibits executive recruiting services and does not represent a significant change from the 2000 rules.
Broker-Dealer	The rule prohibits: 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. The release states that the only change from the 2000 rules is the explicit coverage of persons who perform broker-dealer services but have not complied with SEC broker-dealer registration requirements.

The Prohibited Non-Audit Services Under the SEC's New Rules (continued)	
Legal Services	The rule prohibits providing a service to an audit client that, under the 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. The release states that the SEC does not intend to prohibit tax services in countries where such services must be provided by lawyers, and will also allow exceptions for other legal servies that would not be considered to be "legal services" in the U.S.
Expert Services	The rule prohibits expert services–such as providing expert testimony or opinions–where the purpose of the engagement is to advocate the client's position in an adversarial proceeding or where the accountant is part of the "team" that "has been assembled to advance or defend the client's interests" in an adversarial proceeding. The rule release states that the auditor may be engaged by the audit committee or its legal counsel to perform internal investigations or other "fact finding engagements" and may provide factual testimony on "positions taken or conclusions reached during the performance of any service." The release also makes clear that this prohibition on expert services does not restrict tax services.

As to five of these services—bookkeeping; financial information systems design and implementation; appraisal, valuation, fairness opinions, and contribution-in-kind reports; actuarial; and internal audit outsourcing—the rules state that the services may not be provided unless it is reasonable to conclude that the results of the service will not be subject to audit procedures during an audit of the client's financial statements.

There is a rebuttable presumption that the services are subject to audit procedures. The SEC release states that an example of a situation where it would be reasonable to conclude that the results would not be subject to audit procedures is where an accounting firm provides a prohibited service to a parent/investor affiliate of the client (or an entity in the mutual fund complex), but the accounting firm is not the auditor of the affiliate.

To the extent that some of the prohibitions are new, such services are prohibited as of May 6, 2003, although services being provided pursuant to contracts in place as of May 6 may continue for up to 12 months (as long as they are not materially modified).

Congress and the SEC Concluded — Tax Services Are Permitted, Subject to Pre-Approval

In its final rule release, the SEC sought to fulfill a fundamental legislative goal — that is, to draw a "clear line" between which non-audit services are permitted and which are not. In this connection, the final rule release eliminated confusion regarding tax services that had developed after issuance of the SEC's earlier proposing release. In the final release, the SEC stated in no uncertain terms: "The Commission reiterates its long-standing position that an accounting firm can provide tax services to its audit clients without impairing the firm's independence." The SEC noted, "tax services are unique among non-audit services for a variety of reasons." These include: the complexity of the tax law, the fact that tax returns are subject to IRS review, and the long-standing complementary relationship of tax services and the audit process.

Tax services are the only *permitted* non-audit service that Congress specifically named, in passing the Act, as being subject to the audit committee pre-approval requirements and not included in the prohibited service restrictions. While the SEC had proposed that audit committees and audit firms might need to measure tax services against certain "simple principles" governing auditor independence — such as a prohibition against "auditing your own work" or acting as an "advocate" for the audit client — commentators noted that these principles were too vague to be useful to audit committees in determining whether to pre-approve tax services. The reference to the principles was dropped in the discussion of tax services in the final rules.

There are three caveats to this assessment of tax services. First, the SEC did state that an auditor would impair its independence if it were to provide what is essentially a legal service by representing an audit client before a tax court, district court, or court of claims. Second, the SEC stated that accounting firms may not circumvent the rules by providing a prohibited non-audit service under the guise of "tax service" merely because the service might involve some tax issues. And third, the SEC concluded that one type of tax activity deserves extra scrutiny by the audit committee — namely, situations where the accounting firm recommends a transaction, the sole business purpose of which may be tax avoidance, and the tax treatment of which may not be supported in the Internal Revenue Code and related regulations. Of course, these types of transactions should be avoided whether brought to a company by its independent auditor or any other service provider.

Commentary on Tax Services. The tax services issue was one of the major points of controversy in the recent rulemaking. Tax services have long been aligned with the audit process. Audits have benefited in many circumstances from increased knowledge developed through the inclusion of tax professionals focused on the contemporaneous understanding of client business operations, structure, transactions, and reporting obligations. In addition, tax services provided by a company's independent auditor now are required to be pre-approved by the audit committee, and the fees and services will be disclosed publicly, neither of which is required when tax services are provided by other parties. Thus, we believe that having the audit firm provide the service, subject to audit committee pre-approval, can frequently enhance audit quality, transparency, and efficiency.

That is not to say that a company's audit firm will, in all cases, be the best choice to provide tax services. Companies will continue to make their decisions on selecting tax service providers based on an evaluation of the service provider's quality and capabilities and consideration of the specific service requirement.

Pre-Approval of Audit and Non-Audit Services Provided by the Auditor

The Rules

The rules require that either:

1. An issuer's audit committee pre-approve the specific audit or non-audit engagement to be rendered by the accounting firm, or
2. The engagement to render services is entered into pursuant to pre-approval policies and procedures established by the audit committee, provided that:
   a. The policies and procedures are detailed as to the particular service
   b. The audit committee is informed of each service that is rendered
   c. Such policies and procedures do not include delegation of the audit committee's responsibilities to management

The rule—and the Act—also include a "de minimis" exception for services amounting to less than 5% of total annual fees paid to the firm, but this is only available where the service was "not recognized by the issuer" to be a non-audit service at the time of the engagement, so we expect that the exception will rarely be applicable.

The Act specified in Sections 201(b) and 202 that all audit and non-audit services provided by the independent auditor must be pre-approved by the audit committee. This is consistent with the expanded role of the audit committee in oversight of the financial reporting process and the relationship with the audit firm. Many, but not all, audit committees have been very involved in decisions regarding the scope of services provided by the independent auditors. While audit committees have been responsible for receiving communications from the independent auditors with respect to the scope of services provided to the company, such communications often occurred subsequent to the commencement of the engagement.

The new pre-approval requirements become effective on May 6 for services that are to be performed pursuant to contracts entered into on or after this date. Services that are already in process or that are covered by contracts dated prior to May 6 do not require pre-approval by the audit committee and may continue for up to 12 months (as long as they are not materially modified).

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The Implications

Pre-approval of all audit and non-audit services to be rendered by the independent auditor is one of the important new responsibilities of the audit committee. The Act and the SEC's rulemaking reflect a shift away from the historical relationship among management, the independent auditor, and the audit committee in which management normally retained the accounting firm, negotiated the fees, contracted for other services, and managed the issuer's relationship with the firm. Management will continue to play a key role in the relationship that the issuer has with the accounting firm; however, the audit committee will now play a much stronger role than in the past.

The audit committee will need to develop effective and efficient pre-approval policies and procedures that are reflective of the complexity of the company's business, set the tone for the desired service relationship with its accounting firm, and provide timely information necessary to discharge its responsibilities There is no disputing the enhanced role that audit committees must play in the issuer's relationships with its independent auditors — appointing the auditors, compensating them, and overseeing their work as required by the Act. However, it will be important that audit committees do not become burdened with management responsibilities that prevent them from discharging their key oversight duties, especially oversight of the financial reporting process.

With regard to the audit committee's duty to pre-approve audit and non-audit services, either of the following two pre-approval approaches is equally acceptable to the SEC: general pre-approval of categories of services based on established policies and procedures, or pre-approval on an engagement-by-engagement basis.

A logical starting point for determining how to proceed with pre-approval of services is to compile an inventory of the services that are currently being performed by the accounting firm or have been performed in recent years. The list of such services provided should then be reviewed to determine whether any of the revisions to the SEC's list of prohibited activities require the issuer to engage a separate service provider for services that the accounting firm is no longer permitted to provide.

The inventorying of services also should focus on how extensive the communications protocols will need to be in order to ensure that potential services are identified and submitted for pre-approval or compared with pre-approved service categories before engaging the independent auditors. Appropriate communication processes should be established both within the issuer's organization and the accounting firm's organization.

Each audit committee will need to determine the considerations to factor into its decision-making processes in determining its approach to pre-approval, and in developing its related detailed policies and procedures. There are many factors to consider, and level of importance of each factor may vary from company to company.

Many audit committees have been early adopters of pre-approval policies and procedures. Based on our understanding of their experiences and the requirements set forth in the SEC's new rules, we have developed an audit committee pre-approval process memorandum and worked with an outside law firm to develop a model pre-approval policy, which are included in Appendix A.

Disclosures to Investors of Services Provided by the Auditor

The Rules

Section 202 of the Act requires that issuers disclose in periodic reports and proxy statements non-audit services performed by the auditor. To enhance investors' understanding of the relationships that exist between the company and its independent auditor, issuers will be required to disclose to investors fee information for four categories of services, a description in qualitative terms of the types of services provided for all categories other than audit services, the extent to which certain de minimis services were approved after the fact, and the issuer's pre-approval policies and procedures.

"...because the new disclosures result in greater transparency than under the 2000 rules, the Commission encourages issuers... to adopt the provisions earlier."

The new rules require that issuers disclose the aggregate fees billed in each of the last two fiscal years in each of the following categories (the information below is supplemented by discussions in the SEC's rule release):

1. *Audit Fees* are the fees billed for professional services rendered for: the audit of the registrant's annual financial statements, the review of quarterly financial statements, services that are normally provided by the accountant in connection with statutory and regulatory filings or engagements, and services that generally only the auditor reasonably can provide. This category includes: fees for statutory audits required domestically and internationally (including statutory audits required for insurance companies for purposes of state law), comfort letters, consents, assistance with and review of documents filed with the SEC, Section 404 attest services, other attest services that generally only the auditor can provide, work done by tax professionals in connection with the audit or quarterly review, and accounting consultations billed as audit services, as well as other accounting and financial reporting consultation and research work necessary to comply with generally accepted auditing standards.
2. *Audit-Related Fees* are the fees billed for assurance and related services that are reasonably related to the performance of the audit or review of the registrant's financial statements, and assurance and related services that traditionally are performed by the independent accountant. This category includes, among other things, employee benefit plan audits, due diligence related to mergers and acquisitions, audits of acquired businesses, internal control reviews and assistance with Section 404 internal control reporting requirements, attest services not required by statute or regulation, and consultations concerning financial accounting and reporting matters not classified as audit.

3. *Tax Fees* are the fees billed for professional services rendered for tax compliance, tax advice, and tax planning. The SEC release indicates that this category would capture all services performed by the professional staff in the independent accountant's tax division, except those rendered in connection with the audit.

4. *All Other Fees* are the fees for products and services other than those in the above three categories. Generally, this category would include permitted corporate finance assistance and permitted advisory services.

The above disclosure rules are effective for periodic filings for the first fiscal year ending after December 15, 2003, and in proxy statements that include such periods. However, particularly because the new disclosures result in greater transparency than under the 2000 rules, the Commission encourages issuers who have not previously issued their periodic annual filings to adopt these disclosure provisions earlier. Based on our discussions with the SEC staff, we understand that, with respect to proxy statements for this proxy season, the SEC staff will allow early implementation of the fee disclosure categories, but will expect the data to be provided on a comparative basis consistent with the new rules.

Another acceptable approach would be to file the proxy disclosures in accordance with the existing rules and supplement those disclosures with additional disclosure of the fee data for 2002 using the new categories. If an issuer elects to follow this supplemental approach, the additional disclosure should be labeled as such and be clearly distinguishable from the required information. In any case, proxy statements filed prior to the effective date of the pre-approval provisions of the new rules will not be required to contain disclosure of audit committees' pre-approval policies and procedures.

The Implications

In its 2000 rules, the SEC began requiring registrants to disclose fees paid to their independent accountants for three categories of services: audit, financial information systems design and implementation, and "all other." Ernst & Young recommended to its clients that, to provide greater transparency and to avoid misunderstandings about the nature of non-audit services, they should also disclose the amount of fees included in the "All Other" category that were actually for "audit-related" services. Many issuers followed this recommendation.

In its new rules the SEC decided to require disclosure of the audit-related category of services and added a separate category for tax services. It was broadly recognized by registrants, the SEC, investors, and others that the disclosures under the 2000 rules were quite misleading. Many persons mistakenly believed that the "All Other" category consisted solely of "consulting" services when, in fact, it included many services closely related to the audit or traditionally performed by the independent accountants, such as audit-related and tax services. The SEC's revised rules also require issuers to describe the various types of services that are included in the audit-related, tax, and all other fee categories.

With the disclosure of more detail than before, investors will be able to make more accurate observations. Prior to these revisions in the SEC's rules, this kind of information was not generally available for consideration and evaluation by investors. As a result, investors, academics, and others often focused on the aggregate "All Other" category number and compared it with "Audit Fees," which the SEC had previously defined very narrowly.

As described above, the audit committee should develop pre-approval policies and procedures that it deems suitable for the particular company. The required disclosures of pre-approval policies and procedures by audit committees not only will facilitate investors' understanding of the audit committee's involvement in pre-approving audit, audit-related, tax, and other services but also will facilitate the development of leading practices and fine-tuning of an audit committee's policies and procedures as it learns from the procedures adopted by other companies.

Hiring Members of the Audit Engagement Team

The Rules

Rules previously issued by the SEC and standards issued by the former Independence Standards Board have long addressed the potential for actual or perceived impairment of independence when partners and other members of the audit engagement team accept employment or join the board of directors of an issuer. In its new rule, the SEC has added restrictions, pursuant to Section 206 of the Act. A one-year cooling-off period will now be required before audit engagement team members can accept employment at the issuer in a "financial reporting oversight role." The SEC final rule is broader than the Act, which would have affected only four specific employment positions at the issuer.

The SEC defines people in a "financial reporting oversight role" to be those persons exercising or in a position to exercise influence over the financial statements, and anyone who prepares those statements. This would include 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.

Certain audit engagement team members are exempted from the one-year cooling-off period. These include:

- Persons other than the lead or concurring partner who provided less than 10 hours of audit, review, or attest services.
- Individuals whose employment resulted from a business combination that was not contemplated. (The audit committee must be made aware of the prior employment relationship.)
- Individuals whose employment resulted from an emergency or other unusual situation. The audit committee must determine that the relationship is in the interests of investors. The SEC expects this situation to be very rare.

The one-year cooling-off period begins a year before the date that audit procedures began for the fiscal period that includes the date of employment. For purposes of this computation, audit procedures commence for a fiscal period on the day after the issuer files its annual report covering the previous fiscal period. This requirement is effective only for employment after May 6, 2003, the general effective date of the rules.

Example for a Calendar-Year Company

Files its 2001 Form 10-K	*Files its 2002 Form 10-K*	*2002 Audit Period*	*Cooling-off Period for 2002 Audit Team*
March 15, 2002	March 22, 2003	March 16, 2002 through March 22, 2003	Ends March 23, 2004

In the above example, a 2002 audit team member covered by the rule could not be hired in a financial reporting oversight role position prior to March 23, 2004.

The Implications

Management should work with the independent auditors to determine what positions are appropriately defined as financial reporting oversight role positions. Because the final rule, unlike the proposed rule, restricts employment only at the issuer and excludes affiliates, a limited number of positions will be affected.

Audit committees should review the company's procedures, and should decide how they want to be involved. This may include which decisions require their direct involvement and which require their notification or approval.

Audit Partner Rotation

The Rules

Audit partner rotation provides a fresh look at the company's business and its financial reporting. The accounting profession has recognized its benefits for many years. Under the rules of the AICPA's SEC Practice Section, the lead audit partner could serve in that role for no more than seven years, followed by at least a two-year break in service. The role of a concurring partner also has been a long-standing SEC Practice Section requirement, although there has been no rotation requirement for that partner.

Section 203 of the Act extended the rotation requirement to include the concurring partner. The Act limits both the lead and concurring partners to a maximum of five consecutive years of service in those roles and requires them to rotate off for at least five years.

"The final rules balance the need for a fresh look with the need to always have a competent team of auditors."

In implementing the Act, the SEC concluded that the rotation rules should apply to more partners than just these two. Its initial rule proposal was very broad—extending to every partner on the audit engagement team around the world, except for those serving truly insignificant subsidiaries. It would have required these partners to rotate off the engagement for five years following a maximum of five years on the engagement. In response to almost uniform commentary that this broad approach could undermine audit quality, the SEC scaled back its proposal. The SEC stated in its release that the final rules balance the need for a fresh look with the need to always have a competent team of auditors. The rules do this by weighing the extent to which the partners have responsibility for decisions on accounting and financial reporting issues and the extent of their relationships with senior management at the parent/corporate level.

For purposes of the rotation requirements, the SEC defined "audit partner" as a partner who is a member of the audit engagement team and who either has responsibility for decision-making on significant auditing, accounting, and reporting matters that affect the financial statements or maintains regular contact with management and the audit committee. The definition does not include 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. The definition also does not include tax partners and other specialists who participate in certain areas of the audit.

The definition includes the following persons:

1. The "lead partner": the lead or coordinating audit partner having primary responsibility for the audit or review.
2. The "concurring or reviewing partner": 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

that 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.

3. Other audit engagement team partners who provide more than 10 hours of audit, review, or attest services in connection with the annual or interim consolidated financial statements of the issuer or a registered investment company at the registrant or parent company level.

4. 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.

The lead partner and the concurring partner will be permitted to serve a maximum of five consecutive years with a five-year time out before resuming an "audit partner" role. All other audit partners will be permitted to serve a maximum of seven consecutive years with a two-year time out. Thus, the rules would permit a partner to spend two years on the audit engagement gaining familiarity with the company and its business and financial issues and then serve for five years as the lead partner.

The rule can be summarized as follows:

Partner Rotation Requirements

Lead Partner	*Concurring or Reviewing Partner*	*Other Engagement Team Partners*
Five consecutive years on	Five consecutive years on	Seven consecutive years on
Five-year time-out	Five-year time-out	Two-year time-out

The audit partner rotation requirements start on the first day of the issuer's fiscal year beginning after the May 6, 2003, effective date. In each situation, the rotation would be required for the first quarter's Form 10-Q.

For example:

Issuer with a June 30 year-end	*Issuer with a December 31 year-end*
Rotation is effective for the year ending June 30, 2004	Rotation is effective for the year ending December 31, 2004

To avoid wholesale changes occurring all at once, the SEC provided for a transition to the new rules. The requirements for concurring partners (but not for lead partners) on domestic issuers are deferred for one year. For partners in the lead and concurring roles, prior years of service are counted. All other audit partners subject to the requirements, including all foreign partners, receive a "fresh start," such that no prior years of service count against the new maximum years of service.

The Implications

The audit committee always should understand the independent auditor's staffing, and be satisfied that the engagement team collectively possesses the experience and competence to perform a high-quality audit.

Ernst & Young is supportive of the new requirements and has historically imposed a more rigorous approach to partner rotation than required by the profession. We have approached rotation under the existing seven-year maximum term with the understanding that the successor lead partner would serve for seven years (rather than only for the two-year required break in service), and have permitted an earlier return only when unforeseen events necessitated doing so. Also, we have had a formal program for assigning lead audit partners and concurring review partners, including (among other things) the involvement of our National Professional Practice group.

As we are revising our own policies for implementation of the new rules, we are considering those situations where it might be appropriate to go beyond the new minimum requirements. At the same time, we recognize the importance of continuity to audit quality and the need to have the right resources on an audit. In advance of the SEC's rulemaking, we initiated a formal process for implementing the eventual new requirements. A key element of the process involves communications among the current audit engagement team partners, our national and local leadership—and, most importantly, the audit committee.

Communications from the Auditor to the Audit Committee

The Rules

Although generally accepted auditing standards already require the independent auditor to make sure that various matters are communicated to the audit committee, the SEC, pursuant to Section 204 of the Act, has issued new rules that require the independent auditor to make certain timely communications to the audit committee.

The SEC's rules require communication prior to the filing of the audit report of (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 ramifications of the use of such alternative disclosures and treatments along with the treatment preferred by the independent auditor, and (3) other written communications between the independent auditor and the management of the issuer or registered investment company that are material to the financial statements, such as any management letter or schedule of unadjusted differences.

The new requirements are effective for audits of fiscal years ending after December 15, 2003.

The Implications

Although the SEC's new requirements do not represent a significant change in practice, we do believe that the required communications are very important. The new rules are one more building block in the changing relationship between the audit committee and the independent auditor—the change to a direct relationship. As the SEC states in the summary of its release on the new independence rules, "the final rules recognize the critical role played by audit committees in the financial reporting process and the unique position of audit committees in assuring auditor independence."

In our view, the final rules are appropriate and the required communications are essential to the audit committee/independent auditor relationship. We believe that audit committees should make oversight of the financial reporting process their top priority and allocate sufficient time during their meetings to fully discharge these responsibilities.

In our comment letter to the SEC on its rule proposal, we recommended that communications from management to the audit committee (in addition to communications from the audit firm) on the required matters should satisfy the new requirements, but the SEC did not make that change in finalizing its rules. The rationale for our comment was that management, as the preparer of the financial statements and related disclosures, bears the primary responsibility for these matters. Although we embrace the new direct relationship with audit committees and believe financial reporting will improve as a result of such changes, we believe that the best results will be achieved when management, the audit committee, and the independent auditors all work closely together while fulfilling their unique roles in the financial reporting process.

Unique Considerations for Investment Companies

The SEC's new rules contain a number of provisions that are unique to investment companies. Some of them are quite complex. We will summarize them briefly.

In its 2000 rules, the SEC established the concept of the "investment company complex." The auditor of a fund generally must be independent of all other entities in the complex. The complex includes:

- The registered investment company audit client (fund)
- Its investment advisor
- Any entity controlled by or controlling the advisor
- Any entity under common control with the advisor that is a registered investment advisor or provides certain services to the fund or any registered advisor
- All other registered or unregistered funds advised by an investment advisor in the complex

Under the SEC's new rules, the fund's audit committee must pre-approve non-audit services provided not only to the fund but also to the advisor and other entities in the complex, where such entities provide ongoing services to the fund and the accountants' services have a direct impact on the fund's operations or financial reporting.

For example, if the fund's custodian, which is under common control with the advisor, asked the auditor to perform procedures related to the security settlement function, that would require pre-approval. However, providing advisory services to the parent of the advisor that are unrelated to the asset management operations would not require pre-approval.

For all other non-audit services to entities within the complex (i.e., those that do not have a direct impact on the fund), the SEC requires the accountant to disclose to the audit committee annually such services and related fees.

The new rules require funds to disclose in their annual proxy and Form N-CSR fee information for each of the last two fiscal years, including Audit Fees billed, and the bifurcated Audit-Related, Tax and All Other Fees as:

- Fees for services rendered to the registrant
- Fees required to be pre-approved by the fund audit committee (as discussed above)

Funds also must disclose aggregate fees billed by the auditor for services rendered to the fund and the fund's advisor, and any entity controlling, controlled by, or under common control with the advisor that provides ongoing services to the registrant for each of the last two fiscal years. This is the same as the disclosure requirement under the 2000 rules (which, however, only required single-year disclosure). Funds also must disclose whether the audit committee considered whether the provision of those non-audit services that were not required to be pre-approved were compatible with auditor independence.

The new rules also have some other special provisions for investment companies. They prohibit audit partners from rotating from one fund within the complex to another. And the timing of audit committee communications is affected, recognizing that investment companies frequently have common boards, but staggered fiscal year-ends.

Appendix A — Audit Committee Pre-Approval Process Memorandum and Model Pre-Approval Policy

Audit Committee Pre-Approval Process — Overview

Under Section 202 of the Sarbanes-Oxley Act (the Act) and the rules adopted by the SEC on January 22, 2003, audit committees must pre-approve all audit and non-audit services provided by their independent auditor. The SEC's rules provide audit committees with two approaches, which the SEC considers equally valid, in carrying out this responsibility:

- The audit committee may pre-approve the particular service, or
- The audit committee may adopt pre-approval policies and procedures, provided they are "detailed as to the particular service and the audit committee is informed of each service"

These two options are not mutually exclusive, and companies may adopt policies and procedures that require the general approval of certain services and the engagement-by-engagement approval of other services.

Congress and the SEC recognize that there are a wide variety of audit, audit-related, tax, and other services that may be provided by the auditor, subject to audit committee pre-approval, that do not impair auditor independence. In the legislative process, Congress carefully examined this issue and determined that only the non-audit services that are specifically identified in the Act should be prohibited. Other services were not found to raise the same concerns, although (as discussed below) some require more careful review by the audit committee under the SEC rule than do others. Accordingly, it seems appropriate that audit committees adopt policies and procedures that provide for different levels of review, depending on the nature of the service and the level of fees. Moreover, as a practical matter it would be difficult for audit committees to pre-approve every non-audit service engagement on a case-by-case basis.

For all of these reasons, we believe that audit committees generally should adopt policies and procedures that allow them to review and approve certain categories of services, but that also require a specific engagement-by-engagement type of approval for other categories of services. We explain the approach in more detail below.

In providing our views on these important issues, we note that no one approach or set of policies and procedures will meet the needs of all companies. Since the adoption of the Act, a number of companies have begun the process of adopting pre-approval policies and procedures. While these procedures have varied considerably, our experience suggests that there are significant benefits in having such policies and procedures in place. The nature and extent of the review that audit committees should give to non-audit services, and the types of policies or parameters for non-audit services that should be established, depend on many factors, including the background and experiences of the particular audit committee members, and the company's history of using the independent auditor to perform certain non-audit services.

Notwithstanding the particular facts and circumstances of any specific company and its audit committee, the most important point is: all audit committees, no matter what the size of the company or the sophistication and experience of the committee members, should engage in a thorough discussion with their auditor and company management about these matters. No audit committee should pre-approve a non-audit service when there is uncertainty about the appropriateness of the service, or where there is a concern that independence might be impaired.

However, in considering these matters, audit committees can find assurance in the fact that there is a precise listing of proscribed services and that the auditor's reputation for independence, objectivity, and ethical behavior is key to its ability to function as an independent accountant. Accordingly, accounting firms should have adopted safeguards to prevent potential impairment of their independence and to detect in a timely manner those matters that without corrective action may impair independence. Audit committees should inquire about these safeguards and how they assist in helping to assure that prohibited services are not provided to SEC audit clients.

Policies and Procedures that Distinguish Between Different Types of Services

Under the Act and the SEC rules, most companies should be comfortable in adopting policies and procedures that allow the audit committee annually to pre-approve categories of audit and audit-related services, as well as most tax services and certain other services. As for services outside of these categories, audit committees generally should approve the services on an engagement-by-engagement basis.

First, audit and audit-related services require a minimal level of consideration relating to pre-approval because they have not been thought to raise independence concerns. In particular, "audit" services—that is, those services whose fees are disclosed as "audit fees" in the proxy statement rules—are defined as services "that are normally provided by the accountant in connection with statutory and regulatory filings or engagements," and services that "generally only the independent accountant reasonably can provide." Similarly, services that are defined as "audit-related" constitute services that "are reasonably related to the performance of the audit or review of the registrant's financial statements," including assurance and related services that traditionally are performed by the independent accountant. These services generally improve audit quality and do not impair independence. In other words, audit-related services are, by definition, not the types of "consulting" services that have given rise to concern about non-audit services in recent years.

Second, most *tax services*, such as tax return preparation and most types of tax planning, generally have been viewed as routine and non-controversial. The SEC's final rule release states: "The Commission reiterates its long-standing position that an accounting firm can provide tax services to its audit clients without impairing the firm's independence." The release also notes that many persons who commented on the rule proposal had contended that allowing the auditor to perform tax services "both enhances the quality of the audit and provides greater independent oversight over the provision of tax services than would occur if a non-audit firm were engaged to provide these services." The final release cites comments indicating that certain "principles" of auditor independence, prohibiting the auditor from "auditing its own work" or serving as the client's "advocate," are too vague and potentially misleading to be useful in analyzing the appropriateness of tax services. However, we believe that the audit committee should consider if the audit firm is best positioned to provide the most effective and efficient service for reasons such as its understanding of the company's business, people, culture, accounting systems, risk profile, and similar factors. This type of analysis is particularly significant for companies that operate internationally or are decentralized, where the company might be in need of the audit firm's services.

The SEC's final release states that close scrutiny is required for a specific type of tax service—tax transactions that are "recommended by the accountant, the sole business purpose of which may be tax avoidance and the tax treatment of which may not be supported in the Internal Revenue Code and related regulations." We would recommend that the audit committee not approve such transactions.

Third, for services in the *"All Other"* fee-disclosure category (which generally are advisory-type services), we believe that some services are routine, and thus may be pre-approved generally, while non-recurring services should be approved on an engagement-by-engagement basis.

Policies and Procedures that Take into Consideration the Amount of Fees

As to all services, we believe that the level of fees should be taken into consideration in at least two ways. *First*, the audit committee might appropriately set a particular fee level at which all non-audit service engagements—no matter what the nature of the service—must be specifically pre-approved (either by a designated member of the committee, such as the chairperson, or by the full committee). If a fee-based policy is established, the pre-approval fee amount may vary based on the size of the company and the type of service.

Second, the policies and procedures might require that the audit committee be mindful of the overall relationship between the total amount of fees for audit, audit-related, and tax services and the total amount of fees for all other permissible non-audit services. There is nothing in the Act or in the SEC's rules that mandates a particular ratio of fees. For example, a company would not violate the independence rules merely because its total amount of All Other non-audit service fees exceed its total amount of audit, audit-related, and tax service fees. However, consideration of this factor is clearly appropriate in today's environment.

Model Pre-Approval Policy

Ernst & Young asked Latham & Watkins LLP for assistance in developing Ernst & Young's model policy. A copy of the model policy is attached. Latham & Watkins LLP's assistance in developing this policy does not constitute legal advice. Companies and their audit committees should consult with their own counsel before adopting this or any other pre-approval policy.

Company Name

Audit Committee

Audit and Non-Audit Services Pre-Approval Policy

I. Statement of Principles

Under the Sarbanes-Oxley Act of 2002 (the "Act"), the Audit Committee of the Board of Directors is responsible for the appointment, compensation and oversight of the work of the independent auditor. As part of this responsibility, the Audit Committee is required to pre-approve the audit and non-audit services performed by the independent auditor in order to assure that they do not impair the auditor's independence from the Company. To implement these provisions of the Act, the Securities and Exchange Commission (the "SEC") has issued rules specifying the types of services that an independent auditor may not provide to its audit client, as well as the audit committee's administration of the engagement of the independent auditor. Accordingly, the Audit Committee has adopted, and the Board of Directors has ratified, the Audit and Non-Audit Services Pre-Approval Policy (the "Policy"), which sets forth the procedures and the conditions pursuant to which services proposed to be performed by the independent auditor may be pre-approved.

The SEC's rules establish two different approaches to pre-approving services, which the SEC considers to be equally valid. Proposed services either: may be pre-approved without consideration of specific case-by-case services by the Audit Committee ("general pre-approval"); or require the specific pre-approval of the Audit Committee ("specific pre-approval"). The Audit Committee believes that the combination of these two approaches in this Policy will result in an effective and efficient procedure to pre-approve services performed by the independent auditor. As set forth in this Policy, unless a type of service has received general pre-approval, it will require specific pre-approval by the Audit Committee if it is to be provided by the independent auditor. Any proposed services exceeding pre-approved cost levels or budgeted amounts will also require specific pre-approval by the Audit Committee.

For both types of pre-approval, the Audit Committee will consider whether such services are consistent with the SEC's rules on auditor independence. The Audit Committee will also consider whether the independent auditor is best positioned to provide the most effective and efficient service, for reasons such as its familiarity with the Company's business, people, culture, accounting systems, risk profile and other factors, and whether the service might enhance the Company's ability to manage or control risk or improve audit quality. All such factors will be considered as a whole, and no one factor should necessarily be determinative.

The Audit Committee is also mindful of the relationship between fees for audit and non-audit services in deciding whether to pre-approve any such services and may determine, for each fiscal year, the appropriate ratio between the total amount of fees for Audit, Audit-related and Tax services and the total amount of fees for certain permissible non-audit services classified as All Other services.

The appendices to this Policy describe the Audit, Audit-related, Tax and All Other services that have the general pre-approval of the Audit Committee.* The term of any general pre-approval is 12 months from the date of pre-approval, unless the Audit Committee considers a different period and states otherwise. The Audit Committee will annually review and pre-approve the services that may be provided by the independent auditor without obtaining specific pre-approval from the Audit Committee. The Audit Committee will add or subtract to the list of general pre-approved services from time to time, based on subsequent determinations.

The purpose of this Policy is to set forth the procedures by which the Audit Committee intends to fulfill its responsibilities. It does not delegate the Audit Committee's responsibilities to pre-approve services performed by the independent auditor to management.

The independent auditor has reviewed this Policy and believes that implementation of the policy will not adversely affect the auditor's independence.

II. Delegation

As provided in the Act and the SEC's rules, the Audit Committee may delegate either type of pre-approval authority to one or more of its members. The member to whom such authority is delegated must report, for informational purposes only, any pre-approval decisions to the Audit Committee at its next scheduled meeting.

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* The services listed in the appendices are for illustrative purposes only and may not be applicable to all companies.

III. Audit Services

The annual Audit services engagement terms and fees will be subject to the specific pre-approval of the Audit Committee. Audit services include the annual financial statement audit (including required quarterly reviews), subsidiary audits, equity investment audits and other procedures required to be performed by the independent auditor to be able to form an opinion on the Company's consolidated financial statements. These other procedures include information systems and procedural reviews and testing performed in order to understand and place reliance on the systems of internal control, and consultations relating to the audit or quarterly review. Audit services also include the attestation engagement for the independent auditor's report on management's report on internal controls for financial reporting. The Audit Committee will monitor the Audit services engagement as necessary, but no less than on a quarterly basis, and will also approve, if necessary, any changes in terms, conditions and fees resulting from changes in audit scope, Company structure or other items.

In addition to the annual Audit services engagement approved by the Audit Committee, the Audit Committee may grant general pre-approval to other Audit services, which are those services that only the independent auditor reasonably can provide. Other Audit services may include statutory audits or financial audits for subsidiaries or affiliates of the Company and services associated with SEC registration statements, periodic reports and other documents filed with the SEC or other documents issued in connection with securities offerings.

The Audit Committee has pre-approved the Audit services in Appendix A. All other Audit services not listed in Appendix A must be specifically pre-approved by the Audit Committee.

IV. Audit-related Services

Audit-related services are assurance and related services that are reasonably related to the performance of the audit or review of the Company's financial statements or that are traditionally performed by the independent auditor. Because the Audit Committee believes that the provision of Audit-related services does not impair the independence of the auditor and is consistent with the SEC's rules on auditor independence, the Audit Committee may grant general pre-approval to Audit-related services. Audit-related services include, among others, due diligence services pertaining to potential business acquisitions/dispositions; accounting consultations related to accounting, financial reporting or disclosure matters not classified as "Audit services"; assistance with understanding and implementing new accounting and financial reporting guidance from rulemaking authorities; financial audits of employee benefit plans; agreed-upon or expanded audit procedures related to accounting and/or billing records required to respond to or comply with financial, accounting or regulatory reporting matters; and assistance with internal control reporting requirements.

The Audit Committee has pre-approved the Audit-related services in Appendix B. All other Audit-related services not listed in Appendix B must be specifically pre-approved by the Audit Committee.

V. Tax Services

The Audit Committee believes that the independent auditor can provide Tax services to the Company such as tax compliance, tax planning and tax advice without impairing the auditor's independence, and the SEC has stated that the independent auditor may provide such services. Hence, the Audit Committee believes it may grant general pre-approval to those Tax services that have historically been provided by the auditor, that the Audit Committee has reviewed and believes would not impair the independence of the auditor, and that are consistent with the SEC's rules on auditor independence. The Audit Committee will not permit the retention of the independent auditor in connection with a transaction initially recommended by the independent auditor, the sole business purpose of which may be tax avoidance and the tax treatment of which may not be supported in the Internal Revenue Code and related regulations. The Audit Committee will consult with the [Senior Tax Officer] or outside counsel to determine that the tax planning and reporting positions are consistent with this policy.

Pursuant to the preceding paragraph, the Audit Committee has pre-approved the Tax services in Appendix C. All Tax services involving large and complex transactions not listed in Appendix C must be specifically pre-approved by the Audit Committee, including: tax services proposed to be provided by the independent auditor to any executive officer or director of the Company, in his or her individual capacity, where such services are paid for by the Company.

VI. All Other Services

The Audit Committee believes, based on the SEC's rules prohibiting the independent auditor from providing specific non-audit services, that other types of non-audit services are permitted. Accordingly, the Audit Committee believes it may grant general pre-approval to those permissible non-audit services classified as All Other services that it believes are routine and recurring services, would not impair the independence of the auditor and are consistent with the SEC's rules on auditor independence.

The Audit Committee has pre-approved the All Other services in Appendix D. Permissible All Other services not listed in Appendix D must be specifically pre-approved by the Audit Committee.

A list of the SEC's prohibited non-audit services is attached to this policy as Exhibit 1. The SEC's rules and relevant guidance should be consulted to determine the precise definitions of these services and the applicability of exceptions to certain of the prohibitions.

VII. Pre-Approval Fee Levels or Budgeted Amounts

Pre-approval fee levels or budgeted amounts for all services to be provided by the independent auditor will be established annually by the Audit Committee. Any proposed services exceeding these levels or amounts will require specific pre-approval by the Audit Committee. The Audit Committee is mindful of the overall relationship of fees for audit and non-audit services in determining whether to pre-approve any such services. For each fiscal year, the Audit Committee may determine the appropriate ratio between the total amount of fees for Audit, Audit-related and Tax services, and the total amount of fees for services classified as All Other services.

VIII. Procedures

All requests or applications for services to be provided by the independent auditor that do not require specific approval by the Audit Committee will be submitted to the [Title of Management Officer] and must include a detailed description of the services to be rendered. The [Title of Management Officer] will determine whether such services are included within the list of services that have received the general pre-approval of the Audit Committee. The Audit Committee will be informed on a timely basis of any such services rendered by the independent auditor.

Requests or applications to provide services that require specific approval by the Audit Committee will be submitted to the Audit Committee by both the independent auditor and the [Title of Management Officer], and must include a joint statement as to whether, in their view, the request or application is consistent with the SEC's rules on auditor independence.

The Audit Committee has designated the [internal auditor or Responsible Person] to monitor the performance of all services provided by the independent auditor and to determine whether such services are in compliance with this policy. The [internal auditor or Responsible Person] will report to the Audit Committee on a periodic basis on the results of its monitoring. Both the [internal auditor or Responsible Person] and management will immediately report to the chairman of the Audit Committee any breach of this policy that comes to the attention of the [internal auditor or Responsible Person] or any member of management.

The Audit Committee will also review the internal auditor's annual internal audit plan to determine that the plan provides for the monitoring of the independent auditor's services.

IX. Additional Requirements

The Audit Committee has determined to take additional measures on an annual basis to meet its responsibility to oversee the work of the independent auditor and to assure the auditor's independence from the Company, such as reviewing a formal written statement from the independent auditor delineating all relationships between the independent auditor and the Company, consistent with Independence Standards Board Standard No. 1, and discussing with the independent auditor its methods and procedures for ensuring independence.

Appendix A

Pre-Approved Audit Services for Fiscal Year 200X*

Dated: , 200X

Service	Range of Fees
Statutory audits or financial audits for subsidiaries or affiliates of the Company	
Services associated with SEC registration statements, periodic reports and other documents filed with the SEC or other documents issued in connection with securities offerings (e.g., comfort letters, consents), and assistance in responding to SEC comment letters	
Attestation of management reports on internal controls	
Consultations by the company's management as to the accounting or disclosure treatment of transactions or events and/or the actual or potential impact of final or proposed rules, standards or interpretations by the SEC, FASB, or other regulatory or standard setting bodies (Note: Under SEC rules, some consultations may be "audit-related" services rather than "audit" services)	

* The services listed in this appendix are for illustrative purposes only and may not be applicable to all companies.

Appendix B

Pre-Approved Audit-Related Services for Fiscal Year 200X*

Dated: , 200X

Service	Range of Fees
Due diligence services pertaining to potential business acquisitions/dispositions	
Financial statement audits of employee benefit plans	
Agreed-upon or expanded audit procedures related to accounting and/or billing records required to respond to or comply with financial, accounting or regulatory reporting matters	
Internal control reviews and assistance with internal control reporting requirements	
Consultations by the company's management as to the accounting or disclosure treatment of transactions or events and/or the actual or potential impact of final or proposed rules, standards or interpretations by the SEC, FASB, or other regulatory or standard-setting bodies (Note: Under SEC rules, some consultations may be "audit" services rather than "audit-related" services)	
Attest services not required by statute or regulation	
Information systems reviews not performed in connection with the audit (e.g.,. application, data center and technical reviews)	
Statutory, subsidiary or equity investee audits incremental to the audit of the consolidated financial statements	
Closing balance sheet audits pertaining to dispositions	
Review of the effectiveness of the internal audit function	
General assistance with implementation of the requirements of SEC rules or listing standards promulgated pursuant to the Sarbanes-Oxley Act	

* The services listed in this appendix are for illustrative purposes only and may not be applicable to all companies.

Appendix C

Pre-Approved Tax Services for Fiscal Year 200X*

Dated: , 200X

Service	Range of Fees
U.S. federal, state and local tax planning and advice	
U.S. federal, state and local tax compliance	
International tax planning and advice	
International tax compliance	
Review of federal, state, local and international income, franchise, and other tax returns	
Domestic and foreign tax planning, compliance, and advice	
Assistance with tax audits and appeals before the IRS and similar state, local and foreign agencies	
Tax only valuation services, including transfer pricing and cost segregation studies	
Tax advice and assistance regarding statutory, regulatory or administrative developments	
Expatriate tax assistance and compliance	

* The services listed in this appendix might properly be subject to specific pre-approval if such services have not previously been provided by the independent auditor and if they are not provided on a routine and recurring basis. The services listed in this appendix are for illustrative purposes only and may not be applicable to all companies.

Appendix D

Pre-Approved All Other Services for Fiscal Year 200X*

Dated: , 200X

Service	Range of Fees
Risk management advisory services, e.g., assessment and testing of security infrastructure controls	
Treasury advisory services, e.g., review of check-clearing and float-management practices and recommendations regarding potential areas of improvement	

* The services listed in this appendix might properly be subject to specific pre-approval if such services have not previously been provided by the independent auditor and if they are not provided on a routine and recurring basis. The services listed in this appendix are for illustrative purposes only and may not be applicable to all companies.

Exhibit 1

Prohibited Non-Audit Services

- Bookkeeping or other services related to the accounting records or financial statements of the audit client
- Financial information systems design and implementation
- Appraisal or valuation services, fairness opinions or contribution-in-kind reports
- Actuarial services
- Internal audit outsourcing services
- Management functions
- Human resources
- Broker-dealer, investment adviser or investment banking services
- Legal services
- Expert services unrelated to the audit

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