

PricewaterhouseCoopers LLP

International Business Machines Corporation

July 30, 2002

Office of the Chief Accountant
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: PricewaterhouseCoopers/IBM Transaction

Ladies and Gentlemen:

We hereby request that the Staff of the Office of the Chief Accountant (the "OCA Staff") of the Securities and Exchange Commission (the "Commission" or "SEC") advise that, based upon and subject to the matters referred to herein, it will not recommend that the Commission take enforcement action against PricewaterhouseCoopers LLP, any of its subsidiaries or any other firms conducting audit activities outside the United States for SEC registrants under the name "PricewaterhouseCoopers" or derivations thereof or otherwise as part of the PricewaterhouseCoopers network of firms or "accounting firm"¹ (collectively, "PwC")², asserting that PwC is not "independent" based upon the attribution to PwC of the activities of PwC's global management consulting and technology services business (such PwC business, the "Consulting Business") in connection with the sale of the Consulting Business to International Business Machines Corporation ("Buyer"), a current audit client of PwC. The Consulting Business subsequent to its acquisition by Buyer is referred to herein as the consulting division of Buyer.

Legal Analysis

The federal securities laws require that financial statements filed with the Commission by public companies, investment companies, broker-dealers, public utilities, investment advisers and

¹ As such term is defined pursuant to Rule 2-01(f)(2) of Regulation S-X.

² Or any other entity that would be subject to the Commission's independence rules as defined in Rule 2-01(f)(2) of Regulation S-X.

others be certified (audited) by independent public accountants.³ The federal securities laws also authorize the Commission to define “accounting, technical and trade” terms used in the federal securities laws.⁴

The Commission has adopted Rule 2-01 of Regulation S-X regarding independence of accountants.⁵ The general standard set forth in Rule 2-01(b) provides that:

“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 judgment.”⁶

Rule 2-01(b) further provides that:

“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.”

The preliminary note to Rule 2-01 states that, in considering the standard set forth in Rule 2-01(b), the Commission looks to, among other criteria, whether the relationship or the provision of service “creates a mutual or conflicting interest between the accountant and the audit client.”⁷

Rule 2-01(c) applies the standards set forth in Rule 2-01(b) to particular circumstances that are considered to impair an accountant's independence.⁸ For example, Rule 2-01(c)(1) provides that an accountant will not be considered independent if “the accountant has a direct financial interest or a material indirect financial interest in the accountant's audit client . . .” In addition, Rule 2-01(c)(3) provides that:

“An accountant is not independent if, at any point during the audit and professional engagement period, the accounting firm or any

³ See, e.g., 15 U.S.C. 77aa(25), (26), 15 U.S.C. 781, 78q, and 78m, 15 U.S.C. 79e(b), 79j, 79n, 15 U.S.C. 80a-8, 80a-29, 15 U.S.C. 80b-3(c)(1).

⁴ See 15 U.S.C. 77s(a), 15 U.S.C. 78c(b), 15 U.S.C. 79t(a), and 15 U.S.C. 80a-37(a).

⁵ Rule 2-01 has recently been amended. See Revision of the Commission's Auditor Independence Requirements, Exchange Act Release No. 43602, Fed. Sec. L. Rep. (CCH) ¶ 86,406. (Nov. 21, 2000) (effective Feb. 5, 2001).

⁶ 17 C.F.R. 210.2-01(b) (2001). Under Rule 2-01, the term “accountant” includes “any accounting firm with which the certified public accountant or public accountant is affiliated.” *Id.* § 210.2-01(f).

⁷ *Id.* § 2.10.2-01 (para. 2 of Preliminary Note).

⁸ See *id.*

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 the audit client's officers, directors or substantial stockholders.”

The Commission's interpretations of Rule 2-01 are collected in Section 600 of the Codification of Financial Reporting Policies (the “Codification”), entitled “Matters Relating to Independent Accountants.”⁹ Section 602.02.c of the Codification restricts the independent accountant from performing “bookkeeping and related professional services” that might cause a “mutuality of interest” to develop between the auditor and its client. In addition, Section 602.02.e of the Codification addresses business relationships, such as joint ventures, limited partnership agreements, and investments, that may impair an auditor's independence. That section provides, in part, that:

“Direct and material indirect business relationships . . . with a client . . . will adversely affect the accountant's independence with respect to that client. Such a mutuality or identity of interests with the client would cause the accountant to lose the appearance of objectivity and impartiality in the performance of his audit because the advancement of his interest would, to some extent, be dependent upon the client.”

PwC and Buyer desire to obtain assurance that (i) PwC may continue to act as Buyer's independent auditor (regardless of whether the Transactions occur), and (ii) PwC's independence will not be deemed impaired to the extent that Buyer or any departing partner of the Consulting Business or employee of Buyer provides services for, enters into business relationships with, or invests in or accepts investments from, PwC audit clients, pursuant to Rule 2-01¹⁰ or rules that may be promulgated thereunder or any other provisions of the Commission's independence rules.

PwC believes that, regardless of whether the Transactions occur, under the conditions detailed in this letter, it would not have a “mutuality of interest” or a “direct or material indirect business relationship” with, or a “direct financial interest or material indirect financial interest” in any of its audit clients as a result of the activities of Buyer (which activities collectively include, without limitation, the consulting division of Buyer and its employees providing services to, entering into business relationships with and making or receiving investments in or from third parties).¹¹ This conclusion is based on the conditions detailed in this letter, including, among other things, that: 1) neither PwC nor its remaining partners will receive or retain any equity

⁹ Codification of Financial Reporting Policies, Section 600-Matters Relating to Independent Accountants, reprinted in Fed. Sec. L. Rep. (CCH) ¶73,251, et. seq.

¹⁰ Rule 2-01(f)(6) of Regulation S-X.

¹¹ It is understood that the foregoing will not relieve PwC or Buyer of their respective obligations to comply with the Commission's auditor independence rules.

interest in Buyer or the consulting division of Buyer;¹² 2) Buyer will not use the PwC name; 3) PwC will not have any corporate governance or management interest in Buyer or the consulting division of Buyer; 4) there will be no revenue or profit sharing between PwC and the consulting division or any other division of Buyer; 5) shared services between PwC and the consulting division of Buyer will be limited and transitional in nature; and 6) to preserve the independence of PwC in future audits of Buyer, it will be necessary for Buyer to engage an independent auditor to conduct audits and reviews as prescribed in paragraph 14 under “Conditions to No-Action Confirmation” below.

Factual Background

The Consulting Business is currently operated on a global basis by certain member firms of the PricewaterhouseCoopers network of firms. As described in Annex B hereto, PricewaterhouseCoopers International Limited and Buyer have negotiated a definitive Master Stock and Asset Purchase Agreement (the “Definitive Agreement”). Pursuant to the terms and subject to the conditions set forth in the Definitive Agreement, PricewaterhouseCoopers International Limited will use commercially reasonable efforts to cause the PwC firms that had previously agreed to participate in “rollup” transactions to agree to sell their respective consulting businesses to Buyer (such proposed sales and related agreements, the “Transactions”).

Buyer will pay a purchase price for the Consulting Business consisting of cash and securities to be issued (“Buyer Securities”). All Buyer Securities received by the participating PwC firms in connection with the Transactions will be paid only to Consulting Business partners who are transferring to Buyer in connection with the Transactions, in exchange for their ownership interests in their respective firms. Such transferring partners will become employees of Buyer immediately following the closing (the “Closing”, and the date of such Closing, the “Closing Date”) of the Transactions. No PwC firm or its remaining partners will retain any Buyer Securities following the Closing of the Transactions.

Other key terms of the Transactions are:

1. Each participating PwC firm will enter into a five-year non-compete agreement with Buyer as set forth in the Definitive Agreement (the “Non-Compete”).
2. After consummation of the Transactions, there will be no corporate governance, management or direct or indirect financial ties between PwC and Buyer (other than payments relating to certain pension and retirement fund obligations, the transition services arrangements described below, and otherwise as set forth herein and in Annex A hereto).
3. PwC will retain obligations to the transferring Consulting Business partners under certain pension plans, and to the transferring Consulting Business partners and employees under certain retirement benefit and welfare plans.

¹² PwC will receive Buyer Securities (as defined below) on the closing date of the Transactions (as defined below), but will immediately distribute such securities to transferring Consulting Business partners or, in certain limited events, transfer such securities to Buyer in exchange for cash at the closing.

4. PwC and Buyer will indemnify one another and their respective specified employees or partners for losses arising from breaches of representations and warranties (provided that claims in respect thereof are made within two years of Closing), their respective obligations, and the separation of assets and liabilities, in each case on the terms set forth in the Definitive Agreement.
5. To preserve the independence of PwC in future audits of Buyer, it will be necessary for Buyer to engage an independent auditor to conduct audits and reviews as prescribed in paragraph 14 under “Conditions to No-Action Confirmation” below.

Conditions to No-Action Confirmation

PwC and Buyer request that, subject to compliance with the following conditions, the OCA Staff not recommend enforcement action to the SEC as a result of any relationship between PwC and Buyer or based on the attribution to PwC of the activities of Buyer in connection with the Transactions:

1. As a consequence of the Transactions, neither PwC nor its remaining partners will receive or retain any equity interest in Buyer or the consulting division of Buyer.¹³
2. Buyer and the consulting division of Buyer will not be entitled to use the “PricewaterhouseCoopers” name or logo, and neither PwC, Buyer nor the consulting division of Buyer will represent in any publication, advertisement, press release, name plates, office signage, business cards or other similar material that it is the same firm, or controls, manages, governs or is affiliated with the other, or any affiliate, subsidiary or division of the other.
3. PwC and Buyer will maintain separate corporate governance, management, and financial structures and interests including: separate boards of directors, executives, employees, capital, credit lines or facilities, client bases, governing documents, operating policies, financial operations and financial and accounting policies, in each case except to the extent permitted under Rule 2-01(c)(2)(iii) of Regulation S-X. PwC and Buyer will not exert financial or other influence over the other party's corporate governance, management, and financial structures or interests.
4. After the Closing Date, PwC will not (other than with respect to services specified in the last sentence of this paragraph 4) accrue, pay to or receive from the consulting division of Buyer any royalty, interest, dividend or other payment, whether or not tied to the performance of the consulting division of Buyer, except for payments required to be made under the terms of the documentation in connection with the Transactions, which payments are described in Annex A to this letter. Accordingly, PwC and the consulting division of Buyer will not share profits or revenues from consulting or any other engagements or agreements. After the Closing, when providing professional services to the same client, PwC and the consulting division of Buyer will do so only pursuant to

¹³ See footnote 12 above.

separate individual agreements with that client. PwC and the consulting division of Buyer will not enter into prime/subcontractor relationships.¹⁴ However, existing engagements may be completed in accordance with their terms. In addition, either Buyer or PwC may purchase the other's services for its own account in exchange for customary, arm's-length compensation or may agree to supply its services to the other upon demand or otherwise in exchange for such customary, arm's-length compensation, provided that the provision of such services is otherwise permitted under the Commission's auditor independence rules and Federal securities and other laws.

5. PwC and the consulting division of Buyer may, but will be under no obligation to, refer clients to one another. PwC will not designate the consulting division of Buyer as a preferred provider of services, and PwC and the consulting division of Buyer may not pay referral fees or other compensation to each other for referrals to each other nor to any subsidiary, affiliate, employee or agency of the other. PwC and the consulting division of Buyer may not enter into any co- or joint marketing, advertising or similar agreements or arrangements with the other that are inconsistent with this paragraph 5 or paragraphs 2 or 4 or that do not clearly state that PwC and the consulting division of Buyer are separate firms. At the date that all of the offices of the consulting division of Buyer cease to occupy space leased by PwC (as described in paragraph 8 below), the restrictions imposed in this paragraph 5 and paragraphs 4 and 9 (to the extent not otherwise imposed pursuant to the Commission's auditor independence rules) shall cease to be effective.
6. After the Closing Date PwC will continue to provide services (other than services presently offered by the Consulting Business) to clients of the consulting division of Buyer whose engagements are transferred to the consulting division of Buyer under the existing engagement letters with such clients and the consulting division of Buyer will continue to provide services to clients of the PwC business under such existing engagement letters between PwC and such PwC clients.
7. From the date hereof to the Closing Date (and thereafter), PwC may continue to act as Buyer's independent auditor. In addition, after the Closing Date, PwC may be appointed auditor of companies, for the year that includes the Closing Date and years subsequent to the Closing Date, with which the Consulting Business had executed a business alliance or other agreement prior to the Closing Date, provided that such business alliance or other agreement with any such company is transferred to Buyer or expires on or prior to the Closing Date.
8. Buyer and PwC will enter into transition services agreements for certain infrastructure and information services, operations services and other services for a limited duration (as set forth below). Buyer and PwC will also grant each other limited, royalty-free licenses to use certain intellectual property to facilitate the provision of transition services. The services provided under these agreements will have varying terms. The services will be provided under the agreements so long as the consulting division of Buyer is physically

¹⁴ See Rule 2-01(c)(3) of Regulation S-X. See also Office of the Chief Accountant: Regarding Auditor Independence, Letter to Arthur Andersen & Co., February 14, 1989.

separate (to the extent described below) from PwC 's businesses and the charges for the services provided are determined at arm's length (defined as not more than cost) and appropriate provision is made so that confidential information is not communicated between Buyer and PwC. PwC will not receive services from Buyer pursuant to the transition services agreements, and PwC will not make a profit on services provided to Buyer. The term for the provision of the services pursuant to the transition services agreements will in no event be longer than three years after the Closing, though Buyer and PwC will use commercially reasonable efforts to terminate the provision of such services as soon as practicable.

In certain cases, PwC will provide office space to the consulting division of Buyer in premises that will be shared between PwC and the consulting division of Buyer. Buyer and PwC will enter into sublease or license arrangements for all such office space to be transferred to Buyer or currently shared by the Consulting Business with other PwC businesses. Under these arrangements, Buyer will pay its proportionate share of the cost of such space based on the total square footage of each facility used by or allocated to the consulting division of Buyer under the terms of such subleases or licenses and, with respect to related services and capital costs, under the terms of the transition services agreements. The sublease or license arrangements as of the Closing Date with PwC for each space will not extend beyond the term of the lease held by PwC. With respect to new leases for office space, Buyer and PwC individually will enter directly into such leases with a landlord and will not enter into new subleases with each other for office space after the expiration of the leases currently held by PwC. Until such relocations are made, PwC and Buyer will have separate and distinct office signage and their offices will be clearly distinguishable from one another although they may share certain common facilities.

9. Subject to the terms of the Definitive Agreement, including the exhibits thereto (e.g., transition services agreements), PwC will not enter into any separate licensing agreements with Buyer with respect to the intellectual property owned by the consulting division of Buyer, except for the licensing of intellectual property for its own account in exchange for customary, arm's-length compensation consistent with paragraph 4 and this paragraph 9.
10. PwC will consent to any reviews deemed necessary by OCA Staff or an independent party designated by the SEC or the OCA Staff to ascertain that PwC is complying with the conditions herein provided.
11. At the Closing Date, the participating PwC firms will enter into, and thereafter comply with the terms of, the non-compete covenant set forth in Article X of the Definitive Agreement; provided, that PwC will be deemed to have complied with the terms of the Non-Compete if it has used its reasonable best efforts to cause participating firms, and their respective partners and principals, to comply. Notwithstanding the previous sentence, such participating PwC firms may, after five years, provide services otherwise restricted under the Non-Compete, including providing such services to audit clients that file reports with the SEC to the extent permitted by SEC independence requirements or professional standards.

12. PwC may retain certain obligations (i) to the transferring Consulting Business partners under pension plans available to partners of PwC and (ii) to the transferring Consulting Business partners and employees under retirement benefit and welfare plans available to partners and employees of PwC, in each case for the amount of benefits accrued through Closing (such benefits collectively, the “Accrued Benefits”). The length of service of transferring Consulting Business partners and employees subsequent to the Closing would be counted toward the vesting of Accrued Benefits (*i.e.* eligibility to receive payment of those Accrued Benefits to which the partner or employee is entitled), but not for the purposes of accruing additional benefits or for any other purpose. In the event that any transferring Consulting Business partners or employees are promoted, transferred or assigned to an accounting role or financial reporting oversight role at Buyer, PwC will pay in full any financial obligations owing to such persons consistent with the Commission’s independence rules.¹⁵
13. Under the indemnification provisions of the Definitive Agreement, the PwC firms will indemnify Buyer and specified employees thereof for losses arising from (i) breaches of obligations under the Transaction documentation, (ii) liabilities or assets that are not transferred to Buyer in the Transactions, and (iii) PwC’s non-consulting businesses, in each case on the terms set forth in the Definitive Agreement. Parallel indemnities run from Buyer to PwC. The PwC firms also jointly and severally indemnify Buyer for losses arising from the inaccuracy of any representation in the Definitive Agreement, subject to the following:
- the indemnity claim in respect thereof must be made within two years of Closing;
 - indemnity claims in respect thereof amounting to less than \$10,000 will not be considered;
 - no amounts will be payable by PwC in respect of such indemnity until the aggregate indemnified amounts exceed 1% of the purchase price; and
 - no amounts will be payable by PwC in respect of such indemnity to the extent such indemnifiable amounts exceed 12.5% of the purchase price.
14. To preserve the independence of PwC in its provision of audit and review services to Buyer, PwC and Buyer understand that the following will be necessary:
- Buyer will obtain an opinion from Salomon Smith Barney as to the fairness of the Transactions from a financial point of view.
 - With respect to (i) the accounting treatment of the Transactions and (ii) the financial statements of Buyer for each of the three consecutive fiscal years, and in the related interim periods, commencing with the fiscal year in which the Closing

¹⁵ See Rule 2-01(c)(2)(iii) of Regulation S-X.

Date occurs, an independent auditor (determined with reference to the Commission's independence rules) other than PwC will be required to conduct an audit on, and review of, the reporting units (as defined in SFAS 141/142) containing the Consulting Business transferred to Buyer in the Transactions. PwC will be required, in its opinion on Buyer's financial statements for each of these three fiscal years, to place reliance on the work of such independent auditor, and will be required to reference in the corresponding audit report the portions of the audit conducted by such independent auditor.¹⁶

15. PwC and Buyer acknowledge that time is of the essence with respect to the period between execution of the Definitive Agreement (the "Execution Date") and the Closing Date. PwC will complete, and Buyer will cooperate in completing, all necessary votes of its partners within 45 days of the Execution Date (except in the case of delays attributable to local legal or regulatory issues), and PwC and Buyer will use commercially reasonable efforts to cause (subject to necessary regulatory approvals) the Closing Date to occur within 90 days of the Execution Date. Because the Definitive Agreement will fix the commercial terms on which the Transactions will be consummated, PwC (including its individual member firms) and Buyer will not renegotiate such terms of the Transactions (other than adjustments required pursuant to local law or regulation) between the Execution Date and Closing Date.

Certain Confirmations

In connection with its request herein, each of PwC and Buyer, insofar as each item below relates to it, hereby confirms to the OCA Staff that:

1. After the Closing Date, PwC and, with respect to its relationship with its independent auditor or auditors, Buyer will continue to be subject to the independence requirements of the securities laws and the SEC's independence rules and interpretations issued thereunder to the same extent as they were so subject prior to the Closing Date.
2. PwC and Buyer agree to the above conditions. PwC and Buyer further represent to the OCA Staff that they are not aware of any provisions of the agreements described herein or any agreement or instrument referred to therein that is inconsistent with this request for no-action.
3. PwC and Buyer have furnished the OCA Staff with a copy of the penultimate draft of the Definitive Agreement and the ancillary agreements (including without limitation the schedules, exhibits and annexes thereto) and hereby represent to the OCA Staff that the final executed versions of such documents will not differ in any respect material to the matters referred to in this letter from the drafts so furnished.

¹⁶ Accordingly, both audit firms will be required to file their reports in respect thereof with the Commission for each of the three consecutive fiscal years commencing with the fiscal year in which the Transactions are consummated.

Confirmation Requested

Based upon the representations contained herein (including without limitation the Annexes attached hereto) and in the materials provided herewith, and subject to compliance with the foregoing conditions, we hereby request that the OCA Staff advise that, regardless of whether the Transactions occur, (a) the Office of the Chief Accountant will not assert that PwC's independence has been impaired to the extent Buyer or any departing partner or employee of the Consulting Business provides services for, enters into business relationships with, or invests in or accepts investments from, PwC audit clients, and (b) the OCA Staff will not recommend that the Commission take enforcement action that would prevent or limit the ability of Buyer to continue to use the audit and review services of PwC on the basis that PwC is not "independent" pursuant to Rule 2-01 or any other provisions of the Commission's independence rules by virtue of the Transactions, including the activities undertaken or expected to be undertaken during any of the Investigatory Period, the Quiet Period, the Pre-Closing Period or the Post-Closing Period, in each case as described in Annex B hereto. PwC and Buyer acknowledge that the relief requested by this letter in clause (a) above will become effective if the Closing occurs within the period contemplated by paragraph 15 above, but in no event later than 90 days after the date of the issuance by the OCA Staff of the confirmation requested above.

* * * * *

Certain matters described above have not yet been publicly announced. Accordingly, pursuant to 17C.F.R. §200.81(b), we hereby request confidential treatment of the contents of our communications with the OCA Staff with respect to all issues relating to this letter (the "Confidential Material") until a date 120 days after release of your response to us, or such earlier date as the OCA Staff is advised by us that all of the information contained in the Confidential Material has been made public. However, we understand and agree that the letter itself and the text of your response to the letter may be made public immediately. In addition to this request for confidential treatment, we will request, under separate cover, confidential treatment for the transaction documentation and the other materials furnished to you in connection with this letter pursuant to the provisions of 17C.F.R. §200.83.

* * * * *

If for any reason you do not concur with the views expressed in this letter, we respectfully request an opportunity to discuss this matter with the OCA Staff prior to any written response to our letter. If you have any questions or need any additional information concerning the foregoing, please do not hesitate to call Lawrence W. Keeshan at 646-471-6770 or David S. Hershberg at 914-499-4311, or James C. Woolery of Cravath, Swaine & Moore, PwC's outside counsel in this matter, at 212-474-1912, or Peter A. Atkins at Skadden, Arps, Slate, Meagher & Flom LLP, Buyer's outside counsel in this matter, at 212-735-3700.

Sincerely,



Lawrence W. Keeshan
PricewaterhouseCoopers LLP

David S. Hershberg
International Business Machines Corporation

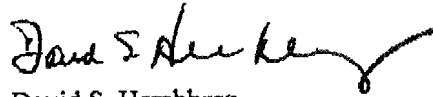
copy to: James C. Woolery, Esquire
Cravath, Swaine & Moore

Peter A. Atkins, Esquire
Skadden, Arps, Slate, Meagher & Flom LLP

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Sincerely,

Lawrence W. Keeshan
PricewaterhouseCoopers LLP



David S. Hershberg
International Business Machines Corporation

copy to: James C. Woolery, Esquire
Cravath, Swaine & Moore

Peter A. Atkins, Esquire
Skadden, Arps, Slate, Meagher & Flom LLP