

AFTER SARBANES-OXLEY  
COMMUNICATING TRANSPARENTLY

*The following paper was presented by Mary Sjoquist, Special Council of the Public Company Accounting Oversight Board (PCAOB) at the American Stock Exchange on September 16, 2003 at the CCI special event "After Sarbanes-Oxley: Communicating Transparently."*

Good evening and thank you for inviting me to participate in this important program. Before beginning, I should point out that the views that I express are my own and not necessarily those of the Public Company Accounting Oversight Board.

In preparing my remarks for this evening, I have to tried to frame my presentation with a view to:

- Responding to the title of the seminar, "After Sarbanes-Oxley—Communicating Transparently
- The characteristics of the sponsors, the Corporate Communications Institute and the Financial Executives' International, and
- The vastness of the subject matter and the need to focus on one or two specific effects of Sarbanes-Oxley during the limited time available this evening. Without that focus, I could surely fill up all of my allotted time by just reciting book, verse and passage of the Act and the resulting effects.

The two primary aspects of transparency, as I see it, are :

- Good disclosure, and
- A significantly improved corporate culture.

I ask myself as I am sure that many of you have

- Could Enron have occurred if the post Sarbanes-Oxley requirements regarding Audit Committees had been in place?
- Could Healthsouth have happened if there had been Board independence, separation of Chairman and CEO positions and whistle-blower provisions and protections in place?
- Would Waste Management have been as devastating if Arthur Andersen and management not been so closely intertwined?
- Would Lernout & Hauspie (the owner of Dictaphone) have occurred if the PCAOB had existed and international auditors had been held to the standards of US GAAP?

I would like to think that the answers to these questions would be in the negative. Sarbanes-Oxley has concentrated the minds in the executive suite and the

boardroom on greater and more transparent financial disclosure, on corporate governance throughout the organization and on new relationships with accounting firms. Although Sarbanes-Oxley provided the impetus for these initiatives, since its passage, the pressure to do a better job has also come from many other sources.

- First from lawyers and auditors. Lawyers and auditors are taking much tougher stances. Lawyers and auditors have more clout with their clients than in the past and clients are sharing more information about their businesses operations. In the past, lawyers and accountants were frequently an after thought when a transaction was in the works and often did not have the time to adequately advise clients on disclosure and other issues.
- Investors are devaluing company stock where the accounting does not appear to be transparent. Transparency has been greatly enhanced following Sarbanes-Oxley in large part through the SEC's new rules including rules regarding the use of Non-GAAP financial measures; rules requiring issuers to maintain disclosure controls and procedures designed to ensure that all material information about the business flows to those individuals responsible for preparing the company's public disclosures; rules requiring disclosure about off-balance sheet arrangements; rules on management's assessment of internal controls; and the rules relating to analyst reports are amongst those that have added to the transparency of financial disclosure and have enabled investors to better make investment decisions.
- Investors are demanding better and more responsive corporate governance. The new rules regarding Codes of Corporate Conduct, Ethics Codes, independence of directors, trading blackout rules and conflicts of interest have all required public companies to at least take steps to comply with the letter of the law and this, in turn, appears to be affecting corporate culture.
- The regulators have also stepped up the pace in terms of their expectations. The SEC has received the badly needed funding to put into place greater enforcement and disclosure review activities and has kept pace with the demanding rulemaking requirements of Sarbanes-Oxley. They expect to and are in the process of hiring 800 additional lawyers, accountants and analysts.
- Likewise, the PCAOB is up and running and has its registration system operational; its inspections and enforcement rules are expected to be adopted by the Board this coming Friday and its first standard on internal controls is expected to be proposed on September 29. The Board's goal is to have 200 employees in house by the end of 2003, most of whom will be inspectors. There is no question that the existence of the PCAOB is causing the rethinking and retooling of auditing firms and their relationships with their clients.

- Post Sarbanes-Oxley and Enron, credit rating agencies are conducting much more thorough due diligence reviews. Expectations of investors and regulators regarding the "guaranty" by credit rating agencies are much more highly elevated post-Enron.
- Insurance costs, particularly D&O insurance, are a strong motivator for the improvements in corporate governance that we are seeing. Costs are skyrocketing particularly where strong corporate governance policies and practices are not in place.
- Auditors are carefully considering when to take on new audit clients and whether to retain old engagements and are doing extensive background checks on both prospective and current clients.

Sarbanes-Oxley and the subsequent external pressures have raised the awareness of the need for honest procedures and also of the liabilities that can be imposed for not following them. It has clearly put an end to the country club atmosphere of Boards where members cared more about their resumes and networking than about guarding against corruption.

We have already seen some momentous changes in the past few months some of which have gone far beyond the requirements of Sarbanes-Oxley and the rules of the SEC.

- One good example is Microsoft's move to expense options—a move some say will make financial statements clearer. Microsoft's move was not as a result of any new regulation.
- Another is Grant Thornton's recent announcement that they are taking the step to not enter into engagements to document internal controls, notwithstanding the fact that there currently is no out-and-out prohibition on an auditor providing such services.
- Of course, another example can be found in the announcement by the WorldCom Board of Directors that it had adopted the provisions of the so-called Breedon report that went way beyond the Act's and the rules' requirements to include provisions such as separating the roles of Chairman and CEO, requiring auditor rotation every 10 years, and amending the certificate of incorporation to include provisions typically left to the discretion of the Board in order that such provisions could only be changed by a vote of the shareholders. As an example of such a provision, the Board voted in favor of amending the certificate of incorporation to include a provision that the Company must elect not less than one new director each calendar year and that no director can serve for more than 10 years except

for the CEO. This, according to the Breedon report will eliminate the danger of "hardening of the arteries of the board collectively."

- Finally, Sarbanes-Oxley appears to have helped foster more accurate corporate reporting. In the 5 months after the enactment of Sarbanes-Oxley, the number of companies submitting financial restatements was disproportionately higher (185) than the number of restatements for the 7 months before its passage (145) and significantly higher than in similar periods in 2000 and 2001.

As Mary Jo White, the past US Attorney in Manhattan recently said: "Sarbanes-Oxley has lasting effects that are here to stay and a lot of what it does is to put teeth into the existing rules—and the teeth matter."

The two substantive areas that I would like to focus on this evening are

- First, the area of internal controls, which, until Sarbanes-Oxley was considered by many to be a fairly mundane topic, and the impact of the SEC's rules and the Board's new standards on corporate transparency, and
- Second, the audit committee and its importance to the scheme of corporate accountability.
- In addition and as time permits, I would also like to bring you up to date on the work of the PCAOB and to take questions that you may have.

## INTERNAL CONTROLS

Internal control is one of the current hot topics at the SEC, the PCAOB, audit firms and public companies. The Act and the rules adopted by the SEC have come under fire for various reasons:

- First, some say that the cost will not outweigh the benefit of increased controls.
- Others say that testing of low level controls would not have deterred the past massive frauds anyway.
- There is concern that putting these rules in place will result in misplaced investor confidence
- Negligence lawsuits will increase.
- Finally, some believe that the requirements will result in confusion in audit committees, senior management and internal and external auditors as to what constitutes an effective internal control system and a significant control deficiency.

In response to these concerns, I believe that no one segment of Sarbanes-Oxley was meant to cure all of the ills. The Act is a quilt and the internal control requirement makes up one of the patches.

Section 404(a) of Sarbanes-Oxley directs the SEC to adopt rules requiring each annual report filed by a company to include an internal control report from management containing:

- A statement of management's responsibility for establishing and maintaining an adequate internal control structure and procedures for financial reporting; and
- Management's assessment, as of the end of the fiscal year, of the effectiveness of the company's internal control structure and procedures for financial reporting.

The SEC has adopted rules implementing Section 404(a).

Section 404(b) requires registered public accounting firms that prepare companies' audit reports, to attest to, and report on, management's assessment of the effectiveness of the company's internal controls in accordance with standards established by the PCAOB. As I indicated earlier, the PCAOB expects to propose the 404(b) standards at a public meeting to be held on September 29.

The potential impact of the requirements for both management and auditors to issue reports related to the issuer's internal controls cannot be understated. Unlike some critics, I believe that increased attention by management on internal controls will reduce the potential for errors in the financial statements, including those due to fraud. The results should be:

- Improvements in internal control structures.
- Strengthening of audits
- Providing important information to investors
- Reducing the chances of material financial statement errors and irregularities.

The attestation by the auditor will provide additional assurance in this regard and, not inconsequentially, improve the quality of audits. Congress made it clear that it considers the internal control attestation to be important to the financial statement audit by prohibiting it from being a separate engagement.

Key points in the 404(a) rules are as follows:

- The Act does not specify a framework for management to assess the effectiveness of the Company's internal controls over financial reporting. In response to public comment that a framework should be prescribed, the SEC's final rules require that management's assessment of the company's internal controls over financial reporting must be based upon a suitable, recognized, control framework that is established by a body or group that has followed due process procedures, including the distribution of the framework for public comment. The best-known framework that currently meets the definition is the framework designed by the Committee of Sponsoring Organizations of the Treadway Commission, (the "COSO Report") published in 1992.
- The report must address both the design of controls and also their operating effectiveness. This means that management must test the controls. Mere inquiry is insufficient. The nature of a company's testing must be based on the company's circumstances, the type of control involved and the significance of the control to the company's financial reporting. In addition, management must maintain reasonable documentation in support of its assertions.
- At the end of the day, management may not conclude that the company's internal control over financial reporting is effective if there are any material weaknesses in internal control.

According to Scott Taub, then the Acting Chief Accountant at the SEC, in a speech on May 29 to the USC School of Accounting, the SEC, prior to Sarbanes-Oxley, as a matter of policy, stated that every public company needed to establish and maintain records of sufficient accuracy to ensure that transactions are appropriately recorded, the internal control system is effectively administered, the financial statements are prepared in accordance with GAAP and the financial statements can be audited. What is different now, according to Mr. Taub, is that management must have a sufficient basis on which to evaluate controls and, as such, the new rules specify that the assessment of a company's internal control must be based on procedures sufficient both to evaluate the design of the controls and to test their operating effectiveness.

Under Section 404(b), auditors are required to attest to management's assertion as to the effectiveness of internal controls on financial reporting. To do so, the auditors must perform enough work to assure that

- Management has designed sufficient testing to evaluate the effectiveness of those controls and put those controls in place.

- Management has performed sufficient testing to evaluate the effectiveness of those controls.
- Management's conclusion about the effectiveness of those controls is conclusive.

Section 103(a)(2)(iii) of the Act requires the auditor to look at the controls themselves and not just management's assessment of the internal control system. It states that auditors must "describe in each audit report the scope of the auditor's testing of the internal control structure and procedures of the issuer, required by Section 404(b).

So how far must the auditors go in order to attest to management's assertions? The PCAOB held a public roundtable on 404(b) on July 29 to air issues prior to proposing our standard and reactions were varied.

- Representatives of the large accounting firms felt that the only way to achieve investor confidence would be to conduct tests of the effectiveness of internal controls themselves in order to be able to attest to management's assertions.
- Representatives of the issuer community seemed to believe that the objective of the auditor's review of internal controls is to assess management's assertion about the effectiveness of the controls and not to test the controls themselves. Costs were cited as a part of the basis for arriving at this conclusion.
- Alan Beller, the Director of the SEC's Division of Corporation Finance indicated that, in assessing effectiveness, the auditor would not have to duplicate everything that management had done but that he believed that the Commission would be very surprised if the auditor's assessment of management's report on internal controls did not also make an independent assessment or evaluation of the internal controls themselves.

In addition to the foregoing issue, the roundtable addressed many other matters which the Board is considering in proposing its internal control standard.

- First, the Board is considering the extent to which the auditor may be able to use the tests performed by management and others to provide some evidence regarding the operating effectiveness of controls. The auditor must, of course, be satisfied that he or she has obtained the principal evidence of overall effectiveness of the company's internal control over financial reporting from tests performed by the auditor. To the extent that internal audit reports directly to the audit committee rather than management, the auditor may be able to place more reliance on the internal audit function.

- The Board is also considering including a requirement that the auditor, before issuing its report, must communicate in writing to the audit committee all material weaknesses and significant deficiencies, or as they were known reportable events. The primary difference between this requirement and past practice is that these were frequently presented orally. Further, significant deficiencies were often brought to the attention of management without the audit committee ever being aware of their existence.
- The Board is considering the question of whether an ineffective audit committee may, in and of itself, be a material weakness in internal controls.
- The Board is considering whether deficiencies of lesser significance than material weaknesses and significant deficiencies should be reported to management in writing with the audit committee being advised that such a communication has been made.

There is a great deal of controversy regarding whether or not and to what extent the company's auditors may assist in the design, testing and evaluation of a company's internal controls. It is clear that the company's auditor cannot perform the evaluation of the effectiveness of the company's internal controls. The SEC's independence rules would prohibit this as it would involve auditors taking on the role of management and/or attesting to their own work.

Scott Taub of the SEC has provided informal advice about the type of assistance that an auditor may provide to an audit client with regard to internal controls without violating the SEC's independence rules. However, management must continue to make all final decisions, exercise its own judgment in performing the analysis and be "in-charge" of the work being done. Having said that, however, it may be appropriate, according to Mr. Taub, for the auditor to

- Develop templates for documenting testing of internal controls
- Make suggestions on what type of tests managers might perform on the internal control systems
- Provide software that helps companies to document internal controls or perform statistical sampling
- Note areas where management may wish to improve controls
- Perform sample selection based on criteria that management has decided should be used.

It would be inappropriate for an auditor to

- Be hired by the company on an outsourced basis for a major part of the work.

- To choose sample sizes
- Decide on tests to perform
- To provide software to conclude as to effectiveness.

Since the PCAOB will be working on a standard on auditor independence in the near future, it is considering the possibility of not providing further guidance as to what auditors may and may not do in assisting companies with their internal controls at this point in time. It is fair to say, however, that auditors and issuers should

- Follow the SEC's independence rules and other guidance that is currently publicly available through SEC speeches, Frequently Asked Questions and Telephone Interpretations
- Have the audit committee specifically approve any separate engagement entered into with the auditor regarding assistance with internal controls.

## AUDIT COMMITTEE

The other area that I would like to focus on this evening is the audit committee. Since the passage of Sarbanes-Oxley, many have said that the audit committee is the lynchpin to the success of the Act. The audit committee is also key to the internal control function within a company and, in particular, to the control environment that is established by the company.

Many public companies have had excellent audit committees, appropriately-staffed and functioning well for years. Others have had audit committees that looked picture perfect on the surface but which totally abdicated their responsibilities. The best examples in this regard were the audit committees of Enron and WorldCom which apparently weren't functioning at all. Sarbanes-Oxley, the SEC's rules and the proposed exchange rules have given teeth to the audit committee and forever changed the way in which audit committees relate to and communicate with management, external auditors, internal auditors and investors.

Let's talk briefly about the scope and impact of these rules.

- First, audit committees must be composed of independent directors and the concept of independence has been considerably strengthened to prohibit directors from generally taking consulting or other fees from the company. Both the NYSE and the Nasdaq proposed rules would require the audit committee to have at least three members.
- Second, the audit committee must have at least one member who is an "audit committee financial expert. This person must have an understanding of GAAP and financial statements; the ability to assess the general application of such principles; experience preparing, auditing or evaluating financial

statements; an understanding of internal controls; an understanding of audit committee functions.

- Third, the rules have expanded the reports that auditors must make to audit committees and thus the corollary responsibility of the audit committee to review and understand the reports. Auditors must provide a timely report of (i) all critical accounting policies and practices to be used by the company; (ii) alternative treatment within GAAP discussed with management; (iii) any management letter, schedule of past adjustments and other material written communications with management.
- Fourth, the audit committee must engage and determine the compensation of the auditors.
- Fifth, the audit committee should determine whether to rotate audit firms and not just to rely on partner rotation. Indeed, as I mentioned earlier, the WorldCom Board of Directors just adopted the proposals in the report to the bankruptcy court prepared by Richard Breedon for the mandatory rotation of audit firms every 10 years.
- Sixth, the audit committee must preapprove all audit services and permissible non-audit services.
- Seventh, the auditors must report directly to the audit committee
- Eighth, audit committees must establish whistle-blower procedures to receive and retain and treat complaints regarding accounting, internal controls and auditing matters.
- Ninth, audit committees must have the authority to engage independent counsel and other advisors when the committee deems it necessary.
- Tenth, audit committees must have a charter which is posted on the company's website the provisions of which are likely to have a significant impact on the committee's behavior. Amongst the duties described in the charter not mentioned above are the duties to: (i) obtain and review annually the independent auditor's report on internal controls; (ii) review all relationships between the auditor and the company; (iii) discuss the annual audit and quarterly reports; (iv) discuss earnings releases, press releases and financial information and earnings guidance provided to shareholders.
- Eleventh, the internal audit function should report to the audit committee and the audit committee should be responsible for the career track and compensation of such persons.
- Twelfth, the audit committee must be effective or risk the possibility of having the company's auditors deem the audit committee ineffective and thus a material weakness in the internal controls of the company.

All of the foregoing requirements are serving to increase the level of corporate communications. Audit committees are meeting more frequently, are holding longer meetings and are reviewing more materials in advance of meetings. Ideally, as a result of the new and enhanced requirements, audit committees will communicate directly with those in charge of internal control without management intervention, audit committees will also communicate directly and more frequently with the company's independent auditors. In doing their diligence, audit committees will speak freely, with individuals throughout the company and not just with the executive office. Audit committees in reviewing earnings and other press releases should also be in direct communications with the company's investor relations, media relations or similar functionaries regarding news to be published. As new and independent savvy directors take on the responsibility of members of the audit committee, they are being faced with difficult questions and hard choices. Auditors, investors and the Board of Directors are going to demand more from the audit committee and, in turn, the audit committee is going to demand more from the executive office, internal control, the auditors and company employees in general. The result should be a greater level of corporate integrity and transparency of disclosure.

## PCAOB

I have alluded to several of the activities that the PCAOB has taken and is in the process of taking but I would like to take a few minutes to provide you with a better overview of who we are and what our mission is.

The PCAOB is the new auditing "watchdog" and Congress gave this dog a very big bark, and some might say "bite" by providing the Board with rather significant powers, subject to SEC oversight.

The PCAOB's broad purpose is to "protect investors by improving the accuracy and reliability of audited financial statements". The goal of accurate and reliable financial statements is, of course, to improve the transparency of financial disclosures.

The PCAOB is to achieve its lofty mission by "overseeing the audit of public companies that are subject to the securities laws, and related matters, in order to protect the interests of investors and further the public interest in the preparation of informative, accurate and independent audit reports for companies the securities of which are sold to and held by and for public investors. The PCAOB is to do this by replacing, superseding and supplanting 60 years of self-regulation and standard-setting by public accounting firms. Needless to say, this is both a major change

and an awesome responsibility. To carry out its mandate, the PCAOB expects to have 200 employees by year end and eventually 300 employees, most of whom will be inspectors. Right now, we stand at approximately 80 full time employees and 30 temporary employees. **[make a pitch for auditors to come to the Board].** So, what is the Board's mandate?

### **PCAOB Roles, Responsibilities, and Powers**

Sarbanes-Oxley gives the Board broad, even sweeping, authority to act in “the public interest and for the protection of investors” to carry out the law’s intent. The Board’s responsibilities fall into four categories:

1. to register public accounting firms;
2. to conduct inspections of registered firms;
3. to conduct investigations and disciplinary proceedings, and enforce compliance with Sarbanes-Oxley, the Board’s rules, professional standards, and securities laws “related to the preparation and issuance of audit reports and the obligations and liabilities of accountants”; and finally,
4. to set standards for auditing public companies, quality control, ethics, independence, and “other standards relating to the preparation of audit reports of public companies.

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#### 1. **Registration** of public accounting firms

Registration with the PCAOB is a new, federal requirement that is necessary for any accounting firm to audit a public company (“issuers” under Sarbanes-Oxley);

- In effect, Sarbanes-Oxley replaces “public accounting firm” in the U.S. securities laws with the term “registered accounting firm”.
  - Firms must apply for registration and supply information, as specifically required by Sarbanes-Oxley, plus additional information as determined by PCAOB (though for the first go-‘round, with very minor exceptions,

the PCAOB's requirements do not go beyond the explicit statutory requirements:

- Registration with the PCAOB is not automatic upon application;
  - the Board is required to determine, within 45 days of a firm's application, whether registration is consistent with the Board's responsibilities under the Act to protect investors and to further the public interest in the preparation of informative, accurate, and independent audit reports for public companies;
- Before registration can be granted, firms must pay a registration fee to offset costs of registering; the fee is based upon the number of public company clients for whom the firm prepares audits and ranges from \$250 for the smallest firms to \$390,000 for the largest firms.

Foreign accounting firms must also register (though they are given some slack):

- 6-mos delay in applying until April 22, 2004, and
- an exclusion from providing certain information if the firm can show that by doing so would violate the confidentiality or other provisions of the laws of their home country.

Why is registration important? Because registration is the predicate for all Board oversight programs (i.e., for the Board's inspection and enforcement programs)

- Nuclear bomb – in the extreme, the Board can revoke a firm's registration and effectively put it out of the business of auditing public companies

## 2. **Inspections (“auditing the auditors”)**

- Purpose: to assess compliance with Sarbanes-Oxley and the rules of the Board, the SEC, and related securities laws;

- Replaces the old peer-review system, which never flunked a single auditor(!), and which even respected auditors considered a sham. The new system is much more potent, if for no other reason than it is independent of the profession. But it is stronger in other ways as well, for example, PCAOB will be able to examine audits under litigation, something that was not possible under the old peer-review system.
  - I should note that there will still be peer reviews, because many states, I believe the number is 31, still require them for their CPAs.
- A continuing program of regular and special inspections
  - Frequency of “regular” inspections depends on the size of the firm (statutory requirement); every year for firms that audit more than 100 public company clients; 1 every 3 years for firms that audit fewer than 100 public company clients;
  - “Special” inspections will be conducted based on our own risk-assessments and other information (e.g., at the request of the SEC or Justice)
- Scope of inspections – not just audits of the audits, but will go beyond auditing engagements and into how auditing firms operate
  - Major attention will be given to the “culture” of the firms, including “tone at/from the top” and compensation policy (e.g., what are the incentives for finding problems?)
    - In the case of “tone-at-the-top”, inspectors will be concentrating on whether the oft-heard, high-sounding rhetoric from the top is actually reaching all levels of the firm; i.e., whether the rhetoric is just rhetoric or whether it is taken seriously by everyone in the firm
    - In the case of compensation, the focus will be on the incentives provided to partners; are they paid for bringing in new, non-audit business, or for conducting audits?
  - In addition to “tone at the top” and “compensation”, we are also looking at:

- Independence/non-audit services;
  - Client acceptance and retention policies
  - Firms' internal inspection program
  - Audit policies and methodologies
  - Foreign affiliates
- PCAOB has already initiated “limited” inspections of the Big 4 firms, but they are rather extensive (9000 hours!); “limited” refers to the fact that the inspections were begun before the firms were registered with the PCAOB, not because they are in any significant way limited in scope.
- Inspectors –inspections (and registration) shop already is and will be PCAOB’s largest; all inspectors are CPAs with recent experience auditing public companies.
  - Inspection reports – Sarbanes-Oxley requires the PCAOB to prepare a report on each inspection, but we must not make any report public for 12 months, giving firms time to fix deficiencies that we uncover.
    - This does not mean that others can not make the report public (e.g., the firm itself, or more likely, a public company that demands to see its auditor’s PCAOB inspection report). I expect that audit committees in making determinations about hiring auditors may want to know whether or not their auditor has been inspected and what the results of that inspection were.
    - The closed report concept also does not prevent the Board from taking enforcement action or referring such actions to the SEC or the Justice Department where it finds violations of law. These actions cannot be remedied in the 12 month period and may, in fact, become public.

The Board's inspection rules are expected to be approved at an open Board meeting to be held on September 19.

**3. Investigations, enforcement, and sanctions** – “where the gloves come off”; when the Board uncovers what appears to be a violation of the rules (or securities laws, SEC rules, or professional standards) it is authorized to conduct thorough investigations. The results of these investigations are the basis for formal

disciplinary proceedings. If a violation is established, the Board may impose a range of sanctions on firms and associated persons of firms:

- Biggest sanction of all: revocation of a firm's registration (dropping a nuclear bomb);
  - Individual auditors can also be sanctioned (e.g., banned from participating in an audit of a public company)
  - Other (lesser) sanctions, including monetary fines, limitations tailored to a particular violation, requirements to retain consultants for particular purposes, and requirements to obtain additional professional education.
- The Board has proposed an extensive set of rules relating to investigations and disciplinary hearings and received a substantial amount of public comment on them. The plan is to consider adoption on Sept. 19<sup>th</sup>.

4. Professional Standards/Standard Setting. Board has unambiguous authority for standard-setting – *auditing*, not accounting, standards, plus standards for auditor independence, ethics, and quality control;

- The auditing profession, through its professional trade group, AICPA, will no longer be able to issue authoritative standards (at least with respect to audits of public companies); instead, Sarbanes-Oxley gave the PCAOB the right to assume this role .
  - The PCAOB decided not to delegate this responsibility (to ASB or any other group) but to undertake standard-setting itself albeit with the help of one or more advisory groups, and of course, its own staff.

I have discussed the internal control standard that the Board expects to propose at an open meeting on September 29. In addition, on that same day, the Board will conduct a Roundtable on audit documentation. Other items high on the Board's list of standard-setting will be a complete review of the independence standards and a determination as to what more needs to be said in light of Sarbanes-Oxley and the SEC's recently-adopted rules.

What has Sarbanes-Oxley told us? It has told us that in the area of financial reporting auditors, issuers, counsel and all others in the stream of public reporting must act in the public interest, a concept that was frequently forgotten in the past. It has attempted to draw the line on corporate governance and on the auditing of financial reports of public companies. But the only way Sarbanes-Oxley will achieve its goal is if public companies and accounting firms change their cultures and remember to act in the public interest. By doing that, auditors and company personnel involved in the financial reporting process are much more likely to arrive at the right answers.