

Opening Statement
Chairman Michael G. Oxley
Financial Services Committee

The Impact of Sarbanes-Oxley
April 21, 2005

Good morning. Today we meet to discuss the impact of the Sarbanes-Oxley Act of 2002. The Committee will hear from the two regulators, Chairmen Donaldson and McDonough, charged with implementing key provisions of the Act. We welcome both of you back to the Committee and look forward to hearing your views on the benefits, and the costs, of Sarbanes-Oxley.

Although the legislation was passed less than three years ago, the benefits to investors and the capital markets have already been quite dramatic. Not entirely measurable in all areas, but dramatic nonetheless.

The primary purpose of the Act was to restore investor faith in the reliability of corporate financial reporting. In this regard, the Act has been an unmitigated success. The audit process has been strengthened. Now subject to rigorous oversight and precluded from offering certain non-audit services to audit clients, accountants have refocused on the audit, achieved greater independence from their clients and are insisting, with success, on more transparent financial reporting.

Replacing decades of ineffectual industry self-regulation, the Public Company Accounting Oversight Board conducts inspections of all registered accounting firms — annually for the largest firms — and has the authority to investigate and discipline accountants and firms that violate Board rules, SEC rules, or securities laws. This oversight by the PCAOB has served, and will continue to serve in my opinion, as an effective deterrent to unethical and illegal conduct.

Oversight of management activities by corporate boards has been significantly improved. Directors, particularly audit committee members, are more engaged, more informed, and more independent of management.

Corporate leaders, subject to stiffer criminal penalties and greater director oversight, are focused on the financial statement like never before. The certification provisions have been successful. Financial statements are more reliable today than they were before the Act was passed.

Does this mean that Sarbanes-Oxley will eliminate fraud altogether? Of course not. No legislation can deliver such a benefit. But we are reducing the opportunities for fraud, making fraud more difficult to commit, and holding accountable those who break the law.

Oxley, page two
April 21, 2005

The most famous, or infamous, section of the Act is of course 404. Nothing is more central to sound financial reporting than the strong internal controls contemplated by Sarbanes-Oxley. I may have heard a complaint or two about the costs, but the benefits have not been disputed. And make no mistake, the costs associated with Section 404 are higher than anyone expected.

That is a cause for concern. I am particularly sensitive to any undue burden on small and mid-size companies, whose compliance costs are higher percentage of total revenues.

The question then becomes, can we achieve the unquestioned benefits of strong internal controls at a more reasonable cost? I believe that we can and that we will. For starters, there seems to be a consensus that 404 costs will be reduced by as much as one-half next year, due to the fact that systems will be in place and documentation will be completed.

I am encouraged by Chairman McDonough's recent comments about costs and his announcement that additional implementation guidance is forthcoming. The PCAOB standard instructs auditors to exercise professional judgment when performing the attestation required by the statute. Upcoming Board inspections will seek to determine whether a one-size-fits-all approach is being used on some audit engagements.

I would also like to commend Chairman Donaldson for his leadership in this area. The Commission has rightly given small companies and foreign companies a delay in complying with 404. The chairman has also organized a useful roundtable discussion on 404 to hear concerns from a broad spectrum of market participants and assembled an advisory committee of smaller public companies.

Finally, I am pleased that there is a consensus, or close to one, on the question of whether legislative modifications are necessary. Congress, regulators, accountants, issuers, and other interested parties generally agree that, to the extent changes are necessary, they can be done in the regulatory context.

I look forward to the testimony.