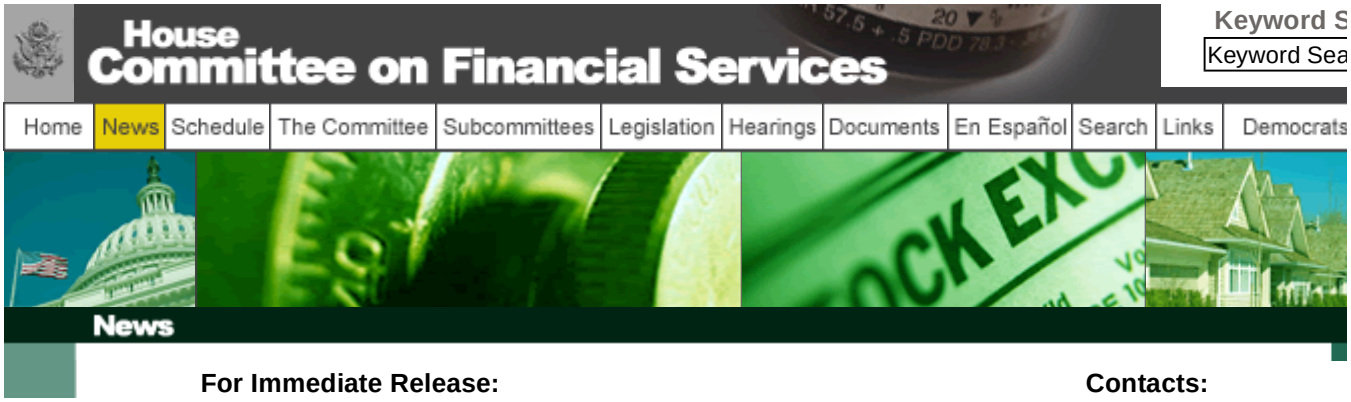

For Immediate Release:
Monday, March 27, 2006

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Baker Subcommittee to Advocate Transparency in Financial Reporting

The Financial Services Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises, chaired by Rep. Richard H. Baker (LA), will convene for a hearing entitled Fostering Accuracy and Transparency in Financial Reporting. The hearing will take place on Wednesday, March 29 at 10 a.m. in room 2128 of the Rayburn building.

Members of the Subcommittee are expected to discuss ways to promote more transparent financial reporting, including current initiatives by regulators and industry.

For the capital markets to operate most efficiently, information about public companies must be understandable, accessible, and accurate. Corporate statements are mathematical summaries meant to convey a company's condition. The four basic documents which must be filed with the U.S. Securities and Exchange Commission (SEC) are at the heart of investor disclosure: the income statement, the cash flow statement, the balance sheet, and the statement of changes in equity.

Among the current initiatives to improve the clarity and usefulness of public company information is a trend away from quarterly earnings forecasting, the use of technology to decrease complexity, and a review of the various accounting standards and how they interact.

Subcommittee Chairman Baker said, "If U.S. markets are to remain on top in an increasingly competitive global marketplace, we need to move away from the complex and cumbersome and explore technological and other methods of enhancing the clarity, accuracy, and efficiency of our accounting system. At the same time, we need to look at whether earnings forecasting and the beat-the-street mentality, which appears to have contributed to some of the executive malfeasance of the past several years, truly serves the best interest of investors or the goal of long-term economic growth."

The corporate scandals several years ago revealed weaknesses in the financial reporting system. While many companies were violating financial reporting requirements, regulatory complexity also may have contributed to some lapses in compliance.

Fraud, general manipulation of statements, and regulatory complexity all contribute to a reduction in the usefulness of financial statements and all may obfuscate the

picture of companies' financial health. A number of recent studies have argued against the practice of predicting future quarterly earnings, concluding that the drive to "make the numbers" can lead to poor business decisions and the manipulation of earnings.

Congress, regulators, and the industry subsequently have assessed financial reporting failures and have reacted with efforts aimed at strengthening the system, including many provisions of The Sarbanes-Oxley Act of 2002.

More recent initiatives by regulators to streamline financial reporting standards and accounting include:

- A Financial Accounting Standards Board (FASB) review of complex and outdated accounting standards;

- The use of principles-based, rather than rules-based, accounting;

- FASB's continued cooperation with the International Accounting Standards Board on the convergence of accounting standards; and

- The use of eXtensible Business Reporting Language, or XBRL, a computer code which tags data in financial statements. The use of XBRL allows investors to quickly download financial data onto spreadsheets for analysis.

Public Companies have been filing financial statements with the SEC since the passage of the Securities Exchange Act of 1934.

Scheduled to testify:

Panel I

- Willis Gradison, Acting Chairman, Public Company Accounting Oversight Board

- Robert H. Herz, Chairman, Financial Accounting Standards Board

- Scott Taub, Acting Chief Accountant, Securities and Exchange Commission

Panel II

- David Hirschmann, Senior Vice President, U.S. Chamber of Commerce

- Marc E. Lackritz, President, Securities Industry Association

- Colleen Cunningham, President, Financial Executives International

- Barry Melancon, President, The American Institute of Certified Public Accountants

- Rebecca McEnally, Director of Capital Markets Policy, Center for Financial Markets Integrity, CFA Institute

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