Speech by SEC Commissioner:
Remarks Before the Institute of European Affairs

by

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Thank you, David. Céad mile Fáilte! Tá áthas orm bheith anseo. Gura maith agaibh go léir inniu.¹ It is an honor to be part of an Institute of European Affairs program. I appreciate the work that the IEA is doing in conducting research and publishing on a vast array of current Irish and European policy issues. Also, of course, in putting together forums like this one. Let me start by saying, as I am required to do, that the views I express here are my own and do not necessarily reflect those of the Securities and Exchange Commission or my fellow Commissioners.

It is truly a pleasure to be with you today in Dublin. I may well be the first SEC commissioner to give an official speech here. But, given Ireland's vibrant economy and its importance in the world and US markets, I am confident that I will not be the last.

Having been impressed from afar at the rapid economic growth that Ireland is experiencing, I am enjoying the opportunity to witness the Celtic Tiger's economic boom first hand. I am pleased that the U.S., through its citizens, corporations, and capital that come to work here, has been welcomed to participate in Ireland's prosperity. The ties between today's Irish and American economies are a natural phenomenon in light of the historically close relationship that our two countries have enjoyed. The Irish-American relationship was born through waves of immigration from Ireland to the U.S. Irish immigrants left for the U.S. at a time of severe economic hardship for Ireland. Today, quite to the contrary, the strength of the Irish economy is attracting a wave of immigrants from other parts of Europe and the world. It is particularly exciting for me, an SEC Commissioner, to see the financial services sector among those that are thriving in Ireland.

Wise economic and regulatory policies seem to be one of the keys to Ireland's economic success. The Heritage Foundation and Wall Street Journal...
annually rate nations according to their level of economic freedom. For 2006, Ireland came in third, behind only Singapore and Hong Kong, and ahead of the United States, which ranked ninth. A white paper issued by the Irish government in 2004 is indicative of Ireland's commitment to economic freedom. The paper, entitled "Regulating Better," set forth six basic, but critically important principles of better regulation: necessity, effectiveness, proportionality, transparency, accountability, and consistency. Underlying the promulgation of these principles was an understanding that a nation's regulatory framework has a very fundamental impact on its competitiveness.

The principles set forth in the white paper are ones to which regulators outside of Ireland would do well to pay heed. So too should regulators be guided in their actions by the following words from the White Paper:

In terms of assessing the need for regulation in an economic context, it is important to assess carefully whether or not the existing situation can be resolved through market mechanisms. Clear criteria should be used to determine whether circumstances justify regulation of particular markets.

Direct intervention by Government always requires careful consideration. The State should avoid the "regulatory impulse" whereby it adopts programmed, default responses to situations that arise, to the exclusion of other possible solutions.

The SEC, in the course of its seven decades, has too often fallen prey to the "regulatory impulse" - jumping to respond with rule-based solutions to any and every problem without checking first to see whether the market might have a better way to solve the problem. Fortunately, the tide is changing in the U.S. also. The SEC's current chairman, Christopher Cox, is taking steps to ensure that the regulations that we adopt meet that standard. Recently, for example, he directed the SEC's General Counsel to carry out a "top-to-bottom review" of the Commission's process for assessing the economic ramifications of its rulemakings. Processes designed to better invite and incorporate the insights of those outside the agency will help to determine whether new rules are necessary and, if they are, will help to generate effective, efficient rules.

Because the effects of regulatory actions often spill over their national borders, it is critical that we seek the insights of all of the parties who will be affected by our rules. That is why I appreciate forums like this in which I can hear from people outside the U.S. about how our rules can be improved. In addition to hearing from those of you who are investors or are among those regulated, I am looking forward to hearing from my counterpart regulators. Particularly, I must tell you that both Ireland and the EU are currently well served by EU Internal Market and Services Commissioner Charlie McCreevy. Commissioner McCreevy brings a welcome, thoughtful outlook on regulatory issues, and is a genuine pleasure to work with. This is very important to the SEC, because we need to work with and understand the concerns of our fellow regulators, particularly here since the European and American economies are so tightly linked.
The need for a cooperative, mutually respecting regulatory approach has been underlined by the merger negotiations between Euronext and the New York Stock Exchange. The contours of the relationship between regulators are still being worked out. Toward that end, Chairman Cox visited Lisbon earlier this week to meet with the Chairman's Committee of the Euronext regulators. I am confident that we will devise solutions that embody the principles of better regulation that I discussed a moment ago.

Frankly, I find speculation about regulatory turf fights much less interesting than consideration of the strategic business and economic reasons of why the New York Stock Exchange and Euronext are looking to combine. The global capital market is certainly becoming more integrated, but one cannot deny that differences among regulatory regimes affect business decision making.

Some have argued that increased regulatory costs in the U.S. are driving European issuers back to their home markets. In the last four years, more than forty European companies have taken this step. Others may well consider following suit if the SEC eases its rules that govern the deregistration process.

The SEC is actively considering amendments to its deregistration rules. In short -- I dare not bore you with too much detail -- under our current rules a foreign issuer may terminate its registration only if it has fewer than 300 U.S. shareholders. In December of last year the Commission published for comment a proposed rule that would offer additional ways for foreign issuers to deregister.

We received more than fifty comment letters, many from European companies, in response to our proposal. Many comment letters urged the SEC to liberalize the deregistration rules even more than it had proposed to do. A frequent theme was that "qualified institutional buyers," whose expectations and needs are radically different from those of retail investors, should be excluded when counting U.S. shareholders. Alternatively, commenters requested that the SEC increase the maximum percentage of U.S. shareholders that a deregistering company is allowed to have.

We are now considering whether and how to modify the proposed approach in light of the comments that we have received. The need for flexibility for issuers must be balanced, of course, against the needs of American equity investors. In my mind, the proper approach will allow issuers to deregister unless their shareholder base includes a large number of U.S. residents who have availed themselves of the U.S. markets, and thereby bargained for the protections afforded by U.S. registration. We take your concerns about the proposal seriously. We are diligently working to devise an approach that takes them into account without compromising our obligation to protect the interests of American investors.

Calls for liberalization of our deregistration rules intensified in the aftermath of Sarbanes-Oxley. The real culprit seems to be Section 404 of the Act. As you know, Section 404 requires management to complete an annual internal
control report and requires the company's auditor to attest to, and report on, management's assessment. Despite its worthy objectives, implementation of that section has produced many unintended consequences, at great cost and tribulation for companies in the U.S. and abroad. The costs, frankly, took everyone by surprise.

The SEC is committed to addressing those implementation problems. As evidence of this commitment, the SEC has hosted two roundtables over the past two years to hear what went wrong and how the process can be improved. In addition, the SEC has given smaller companies and foreign issuers more time to comply with Section 404 requirements. Most recently, we granted relief from Section 404 to accelerated foreign private issuers that are not large accelerated filers by extending for a year the deadline for an auditor's attestation report. The auditor attestations will first be required in annual reports for fiscal years ending on or after July 15, 2007. These companies must include management assessments of internal controls in their annual reports filed for their first fiscal year ending on or after July 15, 2006.

We also proposed to extend the filing deadlines for non-accelerated filers, both foreign and domestic. Under the proposed extension, they would have to file their management assessments for the first time for fiscal years ending on or after December 15, 2007 and the auditor's attestations on those assessments would first be required for fiscal years ending on December 15, 2008. We also proposed transitional relief for newly public companies, including foreign private issuers listing on a U.S. exchange for the first time. A newly public company would not be required to provide either a management assessment or an auditor attestation report until it has previously filed one annual report with the Commission.

In announcing this most recent package of Section 404 relief, the Commission estimated that 60% of the approximately 1,200 foreign private issuers will benefit from the Section 404 relief. The remaining foreign private issuers are "large accelerated filers," to which both Section 404 requirements already apply.

Many of the problems associated with Section 404 stem from the audit standard adopted by the Public Company Accounting Oversight Board to govern the auditor's role in opining on an issuer's internal controls. The PCAOB is the body that is responsible for overseeing audits of U.S. issuers and the auditors that carry out those audits. The PCAOB was established as part of the Sarbanes-Oxley reforms to oversee U.S. public company audits. It is not a governmental entity - although it might look that way from the nature of the powers it possesses -- but rather is subject to the oversight of the SEC.

The PCAOB's audit standard has made it difficult for auditors to employ professional judgment in assessing internal controls and caused them instead to use a time-intensive, deep-in-the-weeds approach. We hear too many stories of excessive documentation, bottom-up audits, and overly
conservative material weakness determinations. The resulting process diminishes the risk of being second-guessed, but does so by foreclosing the use of reasoned judgment.

The PCAOB is working now to revise the relevant audit standard so that it is shorter, simpler, and allows for more efficient application. Our office of Chief Accountant, under the able leadership of our new Chief Accountant Conrad Hewitt, is working with the PCAOB on revising the audit standard. The process for overseeing the work of the PCAOB is not without its limitations, which make it difficult for the SEC to shape the PCAOB's final standard with the degree of precision that I would like. Nevertheless, I am committed, if necessary, to employing all of the SEC's oversight tools to ensure that the standard gets fixed.

Importantly, the SEC is simultaneously working on guidelines of our own for company management. Absent such guidance, companies have been at the mercy of their auditors and have incurred great costs in satisfying seemingly unreasonable demands from auditors operating under the constraints of the PCAOB's unwieldy audit standard. By providing management with guidance of its own, we hope to restore a healthy balance to the process.

Let me turn finally to the issue of accounting standards. With the new EU-wide mandatory application of International Financial Standards, this is an important period in the history of accounting. Accordingly, as European companies transition to IFRS, many on both sides of the Atlantic are watching. This is the time during which the groundwork must be laid to ensure high-quality standards and consistent application of IFRS across all of the nations in which it is used.

Many are working to ensure the success of IFRS. The International Accounting Standards Board, under the strong leadership of Chairman Sir David Tweedie and Vice Chairman Tom Jones, is working to achieve and maintain consistently high-quality standards with input from the full range of interested parties. Issuers, of course, are on the front lines and face the most difficult challenge of applying IFRS consistently and appropriately in their particular circumstances. I hope that companies are working together in this effort with other similarly situated companies.

Accounting firms also play a critical role in helping to achieve consistent application of IFRS across clients, industry groups, and national borders. To do this, they need to be internally consistent and talk to one another so that differences of interpretation do not develop firm-to-firm. National regulators need to resist the impulse to develop a nationally specific version of IFRS. International organizations - CESR and IOSCO in particular - are facilitating consistent application through, among other things, the development of databases of IFRS decisions by members.

We at the SEC, for our part, are actively participating in the efforts to establish IFRS as a viable and reliable set of accounting standards. Our staff is currently reviewing the filings of foreign issuers that have filed using IFRS.
These filings will enable us to assess IFRS. It is one thing to see a theoretical standard, and quite another to see how it is applied across a broad range of companies.

I have never believed that it is necessary to impose a single set of accounting rules on all participants in the global marketplace in order to allow competition across borders. In fact, due to differences in culture, legal systems, and liability regimes, true equivalence in accounting standards may be an impractical objective, at least in the near future. What is critical, however, is that accounting standards be clearly stated and evenly applied by all nations and companies adopting those standards. Moreover, financial reporting standards must be implemented in such a way that they succeed in serving their intended purpose of protecting investors.

The coherent consistent application of IFRS is an essential prerequisite to the elimination of the reconciliation requirement in the United States. It will take us some time to assess how IFRS is being implemented and enforced, but I am optimistic that we will complete our assessment, well within the 2009 goal for reconciliation, and be able to determine that the reconciliation requirement is unnecessary. Our new Chief Accountant, Conrad Hewitt, is committed to working to achieve this objective as quickly as possible.

I am keenly aware that shareholders ultimately bear the costs of reconciliation - like many of our regulations - and these costs are considerable. For this reason, I am very interested in what appears to be growing European sentiment against requiring reconciliation for U.S. issuers that currently use GAAP in their EU filings. Requiring U.S. companies to reconcile their U.S. GAAP financial statements to IFRS would undermine our efforts towards mutual recognition by senselessly diverting attention and energy from our shared, transatlantic objective of making sure that IFRS succeeds. U.S. GAAP is already an established standard that has proven itself to investors over time. The need for reconciliation disappears when IFRS shows itself to be, like GAAP, a consistently applied, high quality set of accounting standards. It is in everyone's best interest to achieve the elimination of the reconciliation requirement as quickly as possible.

In the meantime, the SEC will work with its European counterparts to improve financial reporting for the benefit of investors everywhere. Just last month, the SEC and the CESR issued a joint work plan, which sets forth goals for cooperation between the regulators. The work plan focuses on the development of high quality accounting standards and achieving consistency and quality for IFRS. The plan sets forth practical ways of bringing this about through formalizing transatlantic channels by which information and experiences with IFRS and US GAAP are shared and specific implementation matters are discussed. The work plan, which will help to form a vital, transatlantic working relationship between regulators, grew out of a meeting between CESR Chairman Arthur Docters van Leeuwen and SEC Chairman Christopher Cox last December.

The deepening of the cooperation between the SEC and CESR is a very
constructive development that will positively influence accounting and auditing practices in the U.S. and in Europe. In addition, both GAAP and IFRS are likely to be improved through the efforts of the Financial Accounting Standards Board and the International Accounting Standards Board.

The FASB and IASB are working to eliminate differences between U.S. GAAP and IFRS consistent with their Norwalk Agreement, the principles of which were reaffirmed in a Memorandum of Understanding entered into earlier this year. The FASB and the IASB have committed to work toward a common set of high-quality accounting standards. Although this is a long-term goal, I have heard encouraging reports about the level of cooperation between the two accounting boards. Indeed, some look to the level of cooperation between the two accounting boards as a model for European and American cooperation more generally. Perhaps we have Tom Jones to thank for this, since, in addition to his work at the IASB, he has served as a trustee of the Financial Accounting Foundation, which oversees FASB, and as a member of FASB's Emerging Issues Task Force.

You have been a very patient audience. I welcome your continued active involvement in our issues, including your questions and comments. My phone and office are always open to you, if you are inclined to pay for an international call or fly to the U.S.! I now look forward to hearing Tom Jones and then would be happy to respond to any comments or questions that you might have for me.

Endnotes

1 English translation: A hundred thousand welcomes. I am happy to be here. Thank you all today.


6This number includes only companies that have deregistered with the SEC and remain publicly traded on a European stock market.


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