MEMORANDUM

To: Members of the Committee on Financial Services

From: Financial Services Republican Staff

Date: December 7, 2023

Subject: Subcommittee on Capital Markets Hearing Entitled "Examining the Agenda of Regulators, SROs, and Standards-Setters for Accounting, Auditing."

On Tuesday, December 12, 2023, at 2:00pm (ET), the Subcommittee on Capital Markets will hold a hearing entitled "Examining the Agenda of Regulators, SROs, and Standards-Setters for Accounting, Auditing." Testifying at the hearing will be:

- **Erica Williams**, Chair, Public Company Accounting Oversight Board ("PCAOB")
- **Richard Jones**, Chair, Financial Accounting Standards Board ("FASB")
- **Robert Cook**, President and CEO, Financial Industry Regulatory Authority ("FINRA")

Public Company Accounting Oversight Board ("PCAOB")

The PCAOB is a non-profit corporation Congress established to oversee the audits of public companies. The PCAOB's responsibilities include: (1) registering public accounting firms; (2) establishing auditing, quality control, ethics, independence, and other standards relating to public company audits; (3) conducting inspections, investigations, and disciplinary proceedings of registered accounting firms; and (4) enforcing compliance with the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley").[1]

The PCAOB was established as a part of Sarbanes-Oxley in response to various accounting scandals of the late 1990s (*i.e.*, Enron, WorldCom, the collapse of Arthur Anderson). Prior to the PCAOB, the accounting profession was self-regulated. Sarbanes-Oxley gives the SEC the authority to oversee the PCAOB's operations, to appoint or remove members, to approve the PCAOB's budget and rules, and entertain appeals of any PCAOB inspection reports or disciplinary actions.[2] The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") established the current funding regime for the PCAOB, which is done primarily through annual accounting support fees. These fees are assessed on public companies (based on their relative average monthly market capitalization) and on broker-dealers (based on their relative average quarterly tentative net capital).

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[1] *See* Securities and Exchange Commission, "Fast Answers: Public Company Accounting Oversight Board (PCAOB)," *available at* https://www.sec.gov/fast-answers/answerspcaobhtm.html.
[2] *Id.*

The PCAOB has the authority to investigate and discipline registered public accounting firms and persons associated with those firms for noncompliance with Sarbanes Oxley. In addition, the PCAOB has investigatory and disciplinary authority relating to the rules of the PCAOB, the SEC, and other professional standards and law governing the audits of public companies, brokers, and dealers. The PCAOB may impose a range of sanctions on an auditor, including censure, monetary penalties, revocation of a firm's registration, and a bar on an individual's association with registered accounting firms.[3]

Financial Accounting Standards Board ("FASB")

Established in 1973, FASB is the independent, private-sector, non-profit organization that establishes financial accounting and reporting standards for public and private companies and non-profit organizations that follow Generally Accepted Accounting Principles ("GAAP").[4]

FASB is recognized by the SEC as the designated accounting standard setter for public companies and other organizations, such as the state Boards of Accountancy and the American Institute of CPAs ("AICPA"), that recognize FASB standards as authoritative.[5] The Board's mission is to establish and improve standards of financial accounting and reporting "to provide useful information to investors and other users of financial reports."[6]

FASB continually updates GAAP and provides guidance for accountants through its standard setting process. FASB's standard-setting process is detailed in their rules of procedure, which describes FASB's operating procedures, the responsibilities of FASB's Chairman and board, and voting protocols.[7] FASB regularly works with the Financial Accounting Standards Advisory Council, the Private Company Council, and other advisory groups when forming the Board's agenda or issuing or implementing changes to GAAP.

The Financial Accounting Foundation ("FAF") supports and oversees FASB. Established in 1972, FAF is the independent, private-sector, non-profit organization responsible for the oversight, administration, financing, and appointment of FASB and the Governmental Accounting Standards Board ("GASB").[8] The collective work of FASB, GASB, and FAF are largely funded through accounting support fees, which FASB collects from issuers and GASB collects from municipal bond broker-dealers.

The seven members constituting a full FASB are appointed by FAF's Board of Trustees for up to two five-year terms and serve full time. FASB members are required to sever any ties with the firms or institutions they served before joining FASB. Chairman Richard Jones began his term as the eighth chairman of FASB on July 1, 2020, and will serve until June 30, 2027.

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[3] *See* PCAOB, "Enforcement," *available at* https://pcaobus.org/Enforcement/Pages/default.aspx.
[4] *See* About the FASB, *available at* https://www.fasb.org/facts.
[5] *Id.*
[6] *Id.*
[7] *See* FASB Standard-Setting Process, *available at* https://www.fasb.org/Page/PageContent?PageId=/about-us/standardsettingprocess.html&isstaticpage=true&bcpath=tff
[8] *See* About the FASB, *available at* https://www.fasb.org/facts/index.shtml.

<u>Financial Industry Regulatory Authority ("FINRA")</u>

FINRA is an independent, not-for-profit organization authorized by Congress to act as a self-regulatory organization ("SRO") over the U.S. securities industry. FINRA traces its roots to 1939, when Congress authorized the National Association of Securities Dealers ("NASD") as an SRO to protect investors and the public interest. The NASD and NYSE Regulation merged to form FINRA in 2007.

Today, FINRA operates under the supervision of the SEC to regulate registered broker-dealers, registered brokers, and crowd funding portals. According to FINRA, they oversee over 624,000 brokers across the United States and analyze billions of daily market events. FINRA is also authorized to propose, implement, and enforce rulemaking.

As an SRO, FINRA is not funded through the congressional appropriations process and largely funds its activities by collecting membership fees from its registered entities. FINRA also collects fines from member firms when it determines a firm has engaged in misconduct or harmed customers. In addition to fees and fines, FINRA maintains financial reserves, which were originally derived from the sale of NASDAQ in 2006. FINRA's 2022 operating expenses were $1.094 billion and expects its 2023 operating expenses to increase by 6%.[9]

[9] *See* FINRA, 2023 Annual Budget Summary (Mar. 2, 2023), *available at* https://www.finra.org/sites/default/files/2023-06/FINRA-2023-Annual-Budget-Summary.pdf.