

**Sarbanes – Oxley**  
**Act of 2002**

Carl Kampel, CPA

***Ellin & Tucker, Chartered***  
***410-727-5735***  
***www.etnet.com***



# Sarbanes-Oxley Act of 2002 Became Public Law (Enacted) on July 30, 2002

## Title I – Public Company Accounting Oversight Board

### Section 101 – Establishment of Board

- Establishes an independent, non-governmental accounting oversight board to oversee the audit of public companies that are subject to the securities laws.



- The board shall be made up of 5 full-time members, only two of which will be certified public accountants. The SEC will appoint members of the Board for a term of 5 years, with one term set to expire each year. Board members will serve no more than two terms, regardless of whether they were consecutive terms.
- Initial board members selected no more than 90 days from the date of enactment (October 31, 2002)
- Not more than 270 days after enactment (April 30, 2003), the board shall have hired additional staff and be ready to operate

### Section 102 – Registration with the Board

- Within 180 days of establishment (January 31, 2003, public accounting firms will be required to register with the Board in order to perform audit functions for any issuer.

### Section 103 – Auditing, Quality Control, and Independence Standards and Rules

- The Board will establish through the adoption of standards, quality control standards and ethics standards to be used by registered public accounting firms in the preparation and issuance of audit reports for any issuer.



- The Board will require registered accounting firms to maintain audit related material for at least 7 years; concurring or second partner review of all audit reports; that audit reports describe the scope of the auditor's testing of the internal control structure and procedures of the audit subject.

## Section 104 – Inspection of Registered Public Accounting Firms

- The Board will conduct a continuing program of inspections of registered accounting firms – every year for firms that provide audit reports to more than 100 issuers annually and once every 3 years for firms that provide audits to fewer than 100 issuers annually. Reports of deficiencies will be reported to the SEC and made available to the public.

## Section 105 – Investigations and Disciplinary Proceedings

- Gives the Board the Authority to conduct investigations, gather testimony and produce documentation through the power of subpoena. Provides the Board with the power to suspend auditors, revoke the registration of accounting firms or impose other penalties for non-compliance in an investigation.



- Monetary penalties for violation of Board rules or securities law are capped at \$100,000 for an individual and \$2,000,000 for an entity. Intentional breaches of the law are capped at \$750,000 and \$15,000,000 respectively.

### Section 106 – Foreign Public Accounting Firms

- Gives the Board authority over foreign accounting firms and sets up a structure for which foreign firms are required to comply with Board requests.

### Section 107 – Commission Oversight of the Board

- Gives the SEC oversight and enforcement authority over the Board and its decisions

### Section 108 – Accounting Standards

- Gives the Board the authority to adopt accounting standards



## Section 109 – Funding

- Establishes that the Board will be funded through fees from private industry.

## Title II – Auditor Independence

### Section 201 – Services Outside the Scope of Practice of Auditors

- Prohibits any registered public accounting firm from providing non-audit services contemporaneously with audit services. Non-audit services include:
  - Bookkeeping or other services related to the accounting records of financial statements of the audit client
  - Financial information system design and implementation
  - Appraisal or valuation services, fairness opinions, or contribution-in-kind reports



- Actuarial services
- Internal Audit outsourcing services
- Management functions or human resources
- Broker or dealer, investment advisor, or investment banking services
- Legal services and expert services unrelated to the audit



## Section 202 – Pre-approval Requirements

- Requires that the issuer's audit committee approve all auditing and non-auditing services provided to an issuer.

## Section 203 – Audit Partner Rotation

- Prohibits a registered public accounting firm from providing audit services to an issuer if the lead audit partner, or the audit partner responsible for reviewing the audit, have performed audit services for that issuer in each of the 5 previous years of that issuer.

## Section 204 – Auditor Reports to Audit Committees

- Requires accounting firms to report to the audit committee of the issuer the methods, practices and policies behind the audit work.



## Section 206 – Conflicts of Interest

- Prohibits an accounting firm from providing audit services for an issuer if the CEO, Controller, CFO, CAO, or any person serving in the equivalent capacity for the issuer was employed in the audit practice of the accounting firm during the 1-year period prior to the audit.

## Section 207 – Study of Mandatory Rotation of Registered Public Accounting Firms

- Requires the Comptroller General to conduct a study on the potential effects of requiring auditor rotation and submit the findings to Congress within 1 year of enactment of this Act.



## Section 209 – Considerations by Appropriate State Regulatory Authorities

- Allows state regulatory authorities to make their own standards for supervising non-registered public accounting firms.

## Title III – Corporate Responsibility

### Section 301 – Public Company Audit Committees

- Allows the SEC to direct the national securities exchanges and national securities associations to de-list any issuer that is not in compliance with Title III of this Act. Establishes that the audit committee of an issuer shall be responsible for appointment and oversight of any audit work performed by an accounting firm.



## Section 302 – Corporate Responsibility for Financial Reports

- Requires the principal executive officer or officers and the principal financial officer or officers, or persons performing similar functions to certify annual and quarterly reports to the SEC.

## Section 303 – Improper Influence on Conduct of Audits

- Prohibits an issuer from providing false or misleading information about the financial condition of the issuer to an accounting firm conducting an audit for the issuer.

## Section 304 – Forfeiture of Certain Bonuses and Profits

- Requires executives of an issuer to forfeit any bonus or incentive based pay or profits from the sale of stock, received in the 12 months prior to an earnings restatement.



## Section 307 – Rules of Professional Responsibility for Attorneys

- Requires the SEC to issue rules within 180 days of the enactment date (January 31, 2003) that will require attorneys that appear or practice before the SEC to report violations of securities laws to the CEO or chief legal counsel and if no action is taken, to the audit committee.

## Title IV – Enhanced Financial Disclosures

### Section 404 – Management Assessment of Internal Controls

- Directs the SEC to issue rules requiring that annual reports filed with the SEC shall state the responsibility of management for establishing and maintaining adequate internal control structure and procedures for financial reporting; and contain an assessment , of the effectiveness of such internal controls.
- Requires that accounting firms also report on internal controls of the client.



## Section 406 – Code of Ethics for Senior Financial Officers

- Directs the SEC to issue rules that require issuers to publicly disclose whether or not that issuer requires senior financial officers to sign a code of ethics. Proposed rules are to be issued within 90 days of the date of enactment (October 31, 2002) and final rules not later than 180 days after that date of enactment (January 31, 2003).

## Section 407 – Disclosure of Audit Committee Financial Expert

- Directs the SEC to issue rules to require each issuer to disclose whether or not they require at least 1 financial expert to serve on their audit committee. Proposed rules are to be issued within 90 days of the date of enactment (October 31, 2002) and final rules not later than 180 days after that date of enactment (January 31, 2003).

## Section 408 – Enhanced Review of Periodic Disclosures by Issuers

- Requires the SEC to review disclosures made to the SEC on a regular and systematic basis for the protection of investors. Such reviews shall include a review of an issuer's financial statements.



## Title VI – Commission Resources and Authority

### Section 601 – Authorization of Appropriations

- Authorizes an additional \$776 million for the SEC for fiscal year 2003 to raise salaries, improve computer systems, and hire additional staff.

### Section 602 – Appearance and Practice Before the Commission

- Gives the SEC the ability to censure persons or entities from appearing or practicing before it that lack of the necessary qualifications to represent others; lack character or integrity, or have engaged in unethical or improper professional conduct; or have willfully violated and provision of the securities laws and regulations issued there under.



## Title VII – Studies and Reports

### Section 701 - GAO Study and Report Regarding Consolidation of Public Accounting Firms

- Directs the GAO to conduct a study and report its findings to Congress within 1 year of enactment date (July 31, 2003) that would examine the reasons for the consolidation of accounting firms since 1989.

### Section 703 – Study and report on Violators and Violations

- Directs the SEC to conduct a study and report its findings to Congress within 6 months of the enactment date (January 31, 2003) regarding the proliferation of violations of securities laws and the penalties therefore.



## Section 704 – Study of Enforcement Actions

- Directs the SEC to conduct a study and report its findings to Congress within 180 days of the enactment date (January 31, 2003), that would review and analyze all enforcement actions by the SEC involving violations of reporting requirements imposed under the securities laws, and restatements of financial statements, over the 5 year period preceding the enactment date to identify areas of reporting that are most susceptible to fraud.



## Title VIII – Corporate and Criminal Fraud Accountability

### Section 802 – Criminal Penalties for Altering Documents (Not limited to public companies)

- Amends the US Code to provide new penalties for the destruction, alteration or falsification of records in Federal investigations and bankruptcy. Penalties for such actions shall include up to 20 years imprisonment, fine, or both.
- Requires any accountant that conducts an audit of any issuer to retain all audit or review paperwork for a period of 5 years. Penalties for violations shall include imprisonment up to 10 years, fines, or both.

### Section 803 – Debts Non-dischargeable if Incurred in Violation of Securities Fraud Laws

- Amends bankruptcy laws to provide that any debt incurred in violation of securities fraud laws shall not be dischargeable in bankruptcy proceedings.



## Section 804 – Statute of Limitations for Securities Fraud

- Changes the statute of limitations for private causes of action that involve claims of fraud, deceit, manipulation or contrivance in contravention of a regulatory requirement concerning the securities laws to 2 years after the discovery of the fact, or 5 years after the violation. This provision shall apply to all proceedings that are commenced on or after the enactment date.

## Section 806 – Protection for Employees of Publicly Traded Companies who Provide Evidence of Fraud

- Provides whistleblower protections for employees of any issuer who willingly provides evidence of fraud or violations of securities laws by that issuer.

## Section 806 – Criminal Penalties for Defrauding Shareholders of Publicly Traded Companies

- Provides that any person who knowingly defrauds shareholders of a publicly traded company shall be fined, or imprisoned up to 25 years, or both.



## Title IX – White-Collar Crime Penalty Enhancements

### Section 902 – Attempts and Conspiracies to Commit Criminal Fraud and Offenses

- Provides that any person who attempts to commit crimes under the title shall be treated under the law as if they had committed the crime.

### Section 903 – Criminal Penalties for Mail and Wire Fraud

- Changes the penalty for mail and wire fraud from a maximum of 5 years imprisonment to a maximum of 20 years imprisonment.



## Section 904 – Criminal Penalties for Violations of the Employee Retirement Income Security Act of 1974 (Not limited to public companies)

- Changes the penalty structure for violations of ERISA from \$5,000 to \$100,000 for violations by an individual; from 1 to 10 years in prison for each violation; and from \$100,000 to \$500,000 for violations by an entity.

## Section 905 – Amendment to Sentencing Guidelines Relating to Certain White Collar Offenses

- Authorizes the U.S. Sentencing Commission to promulgate guidelines or amendments, not later than 180 days after the date of enactment (January 31, 2003), to tighten sentencing guidelines for certain white-collar crimes.



## Section 906 – Corporate Responsibility for Financial Reports

- Requires that each periodic financial report to the SEC be accompanied by a written statement that is signed by the CEO and the CFO of the issuer that certifies that the periodic report containing the financial statements fully complies with securities laws. Penalties for certifying a misleading or fraudulent report shall be a fine up to \$1 million, or imprisonment up to 10 years, or both; penalties for willfully certifying a misleading or fraudulent report shall be a fine up to \$5 million, or imprisonment up to 20 years, or both.

## Title XI – Corporate Fraud Accountability

### Section 1102 – Tampering with a Record or Otherwise Impeding an Official Proceeding

- Provides that anyone who corruptly tampers or obstructs an official proceeding shall be fined or imprisoned up to 20 years, or both.



## Section 1103 – Temporary Freeze Authority for the Securities and Exchange Commission

- Gives the SEC the authority to freeze temporarily any extraordinary payment to an employee of an issuer for up to 45 days if the issuer is under investigation by the SEC. Freeze can be extended to as long as 90 days with the approval of a court.

## Section 1106 – Increased Criminal Penalties Under Securities Exchange Act of 1934

- Increases criminal penalties for violations of the Securities Exchange Act of 1934 from \$1 million to \$5 million for individuals; from 10 years to 20 years imprisonment for each violation; and from \$2.5 million to \$25 million for each entity.

