EMAIL FROM DAVID POVEY IN 2002, FROM THE RMAA LISTSERV – LINKING
RECORDKEEPING, EVIDENCE AND ACCOUNTABILITY, IN THE CONTEXT OF
THE SARBANES-OXLEY ACT 2002 (USA)

To:
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[MESSAGE FROM DAVID POVEY]

Dear Listservers,

Following up on a posting last week about records destruction, Australian records managers
might be interested in reading ARMA's advice about the corporate responsibility legislation that
has recently been introduced in the US. We are in a different situation than the US, but the
public accountancy firms are the same and the audit process is very similar so it is not difficult to
imagine our parliaments at least considering this new legislation when reviewing corporate
responsibility here. I am attaching excerpts from the ARMA advice which has been sent to
ARMA members.

ARMA - Wednesday, August 7, 2002

Legislative Update
Summary of Provisions in H.R. 3763, the Sarbanes-Oxley Act of 2002, Relating to
Documentation H.R.3763, the Sarbanes-Oxley Act of 2002, signed by President Bush on July
30, 2002, attempts to address many of the issues raised by the Enron and Arthur Andersen
matters. The law creates a new oversight board for accounting firms auditing publicly traded
companies. It also addresses auditor independence; corporate responsibility at publicly traded
companies, financial disclosures of publicly traded companies, and conflicts of interests of
financial analysts. The new law also creates protections for "whistleblowers" at publicly traded
companies and imposes new criminal penalties relating to fraud, conspiracy, and interfering with
investigations.

Summary of Provisions Referring to or Involving Records

Several provisions of Sarbanes-Oxley address or refer to certain records.
These are outlined below in the order that they appear in the new law.

Section 101 of the Act establishes the Public Company Accounting Oversight
Board to "oversee the audit of public companies that are subject to securities laws, and related
matters, in order to protect the interests of investors and further the public interest in the
preparation of informative, accurate, and independent audit reports for companies the securities
of which are sold to, and held by and for, public investors."

Section 102 requires accounting firms that desire to "prepare or issue, or to participate in the
preparation or issuance of, any audit report of a publicly traded company" to register with the
Board.

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Background reading
The Board is authorized to establish rules governing these registered accounting firms and to assure that these firms comply with Board rules.

Section 103 requires each registered public accounting firm to, among other things, "prepare, and maintain for a period of not less than 7 years, audit work papers, and other information related to any audit report, in sufficient detail to support the conclusions reached in [the audit report]." See Sec. 103(a)(2).

Section 104 allows the Board to "require the retention by registered public accounting firms for inspection purposes of records whose retention is not otherwise required" under Section 103 or the rules promulgated by the Board. See Sec. 104(e).

Section 105 authorizes the Board to conduct investigations of any act or practice by a registered public accounting firm or an associated person with such firm. See Sec. 105(b)(1). Section 105 also authorizes the Board to "require the production of audit work papers and any other document or information in the possession of a registered public accounting firm or any associated person thereof," that is relevant or material to an investigation by the Board. See Sec. 105(b)(2)(B). Section 105 also authorizes the Board to suspend or bar any individual from association with a registered public accounting firm or to suspend or revoke the registration of any public accounting firm for failure to produce any documents requested. See Sec. 105(b)(3). Section 105 also makes these documents, with limited exceptions, confidential. See Sec. 105(b)(5).

Section 2(a)(4) of the Act defines "audit report" as "a document or other record prepared following an audit performed for purposes of compliance by an issuer with the requirements of the securities laws; and in which a public accounting firm either sets forth the opinion of that firm regarding a financial statement, report, or other document; or asserts that no such opinion can be expressed."

Section 103 defines the scope for audit reports by requiring that each registered public accounting firm describe in each audit report 1) "the scope of the auditor's testing of the internal control structure and procedures" of the publicly traded company and include in the report "the findings of the auditor from such testing," 2) "an evaluation of whether such internal control structure and procedures include maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer, provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer," and 3) "a description, at a minimum, of material weaknesses in such internal controls, and of any material noncompliance found on the basis of such testing." See Sec. 103(a)(2)(A).

Title V of the Act addresses "conflicts of interest that can arise when securities analysts [employed by a broker or dealer engaged in investment banking activities] recommend equity securities in research reports and public appearances."
Section 501 of the Act authorizes the SEC to issue rules that restrict "the prepublication clearance or approval of research reports" of these analysts and define periods during which brokers or dealers participating in public offerings should not "publish or otherwise distribute research reports relating to such securities or to the issuer of such securities." See Sec. 501(a).

Section 501 also requires the SEC to issue rules that "establish structural and institutional safeguards within registered brokers or dealers to assure that securities analysts are separated by appropriate informational partitions within the firm from the review, pressure, or oversight of those whose involvement in investment banking activities might potentially bias their judgement or supervision." [underline added] See Sec. 501(a).

Section 501 defines the research report to mean "a written or electronic communication that includes an analysis of equity securities of individual companies or industries, and that provides information reasonably sufficient upon which to base an investment decision." See Sec. 501(c).

Title VIII of the Act, cited as the "Corporate and Criminal Fraud Accountability Act of 2002," establishes certain penalties for altering certain documents.

Section 802 of the Act amends Chapter 73 of title 18 of the U.S. Code by adding provisions related to the "destruction, alteration, or falsification of records in federal investigations and bankruptcy." Title 18 of the U.S. Code covers "Crimes and Criminal Procedures" and Chapter 73 of title 18 covers "Obstruction of Justice." The provisions in this title and chapter will not be limited to registered public accounting firms, publicly traded companies, or investment banking firms as are other provisions of the Sarbanes-Oxley Act.

One new provision added to Chapter 73 of title 18 of the U.S. Code imposes a fine and/or imprisonment of not more than 20 years for "whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence" an investigation or proceeding by a federal department or agency or any case filed in bankruptcy." See Sec. 802; new section 1519 of title 18 of the U.S. Code.

A second new provision added to Chapter 73 of title 18 of the U.S. Code imposes a fine and/or imprisonment of not more than 10 years for failure of any accountant who conducts an audit of a publicly traded company to "maintain all audit and review workpapers for a period of 5 years from the end of the fiscal period in which the audit or review was concluded." See Sec. 802; new section 1520(a)(1) of title 18 of the U.S. Code. New subsection 1520(b) applies the fine and/or imprisonment to "whoever knowingly violates" the duty imposed on any accountant, leaving some question as to the applicability of this new section of Chapter 73.

New Section 1520(a)(2) requires the SEC to issue a notice of proposed rulemaking within 180 days relating to these new rules, with opportunities for public comment, and anticipates the inclusion in the meaning of workpapers "documents that form the basis of an audit or review, memoranda, correspondence, communications, other documents (including electronic records), which are created, sent, or received in connection with an audit or review and contain conclusions, opinions, analyses, of financial data relating to such an audit or review, which is conducted by any accountant who conducts an audit of [a publicly traded company]."
Section 804 of the Act extends the statute of limitations for securities fraud relating to a private right of action under section 78c(a)(47) of title 15 of the U.S. Code to "2 years after the discovery of the facts constituting a violation; or 5 years after such violation." Section 78c(a) of title 15 of the U.S. Code is found in Chapter 2B, which applies to security exchanges. Section 78c(47) provides a definition for "securities laws." Section 804 of Sarbanes-Oxley extends the statute of limitations to all applicable security laws.

Section 805 directs the U.S. Sentencing Commission to amend the Federal Sentencing Guidelines to ensure that "the enhancements and specific offense characteristics relating to obstruction of justice are adequate in cases where" ... "the destruction, alteration, or fabrication of evidence" are involved.

Section 806 also amends Chapter 73 of title 18 of the U.S. Code by establishing certain "protection[s] for employees of publicly traded companies who provide evidence of fraud." New section 1514A of Chapter 73, entitled "civil action to protect against retaliation in fraud," creates "whistleblower" protections for these employees who, among other things, lawfully "provide information, cause information to be provided, or otherwise assist in an investigation regarding any conduct which the employee reasonably believes" violates specific sections of the U.S. Code or any rules or regulations of the SEC.

Title XI of the Act, cited as the "Corporate Fraud Accountability Act of 2002," adds a new provision to section 1512 of title 18 of the U.S. Code. Section 1512 is also in Chapter 73 of title 18 and specifically addresses tampering with a witness, victim, or an informant. This new provision added by the Sarbanes-Oxley Act imposes a fine and/or imprisonment for not more than 20 years for anyone who "corruptly alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding" or "otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so."

Summary of Key Provisions

In summary, Sarbanes-Oxley imposes new safeguards on public accounting firms that want to audit publicly traded companies, publicly traded companies, and firms with securities analysis and investment banking functions.

The Act also amends Chapter 73 of title 18 of the U.S. Code dealing with obstruction of justice within the context of crimes and criminal procedure. These amendments, which may apply to any person who violates the new sections to Chapter 73, are summarized:

Imposes a fine and/or imprisonment of not more than 20 years for "whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence" an investigation or proceeding by a federal department or agency or any case filed in bankruptcy. See new Section 1519 of title 18 of the U.S. Code.
Imposes a fine and/or imprisonment of not more than 10 years for the failure of any accountant who conducts an audit of a publicly traded company to "maintain all audit and review workpapers for a period of 5 years from the end of the fiscal period in which the audit or review was concluded." See new Section 1520 of title 18 of the U.S. Code. But note that new subsection 1520(b) applies the fine and/or imprisonment to "whoever knowingly violates" the duty imposed on any accountant, leaving some question as to the applicability of this new section of Chapter 73.

Creates "whistleblower" protections for employees who, among other things, lawfully "provide information, cause information to be provided, or otherwise assist in an investigation regarding any conduct which the employee reasonably believes" violates specific sections of the U.S. Code or any rules or regulations of the SEC. See new Section 1514A of title 18 of the U.S. Code.

Imposes a fine and/or imprisonment for not more than 20 years for anyone who "corruptly alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding" or "otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so." See amended Section 1512 of title 18 of the U.S. Code.

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