

Polishing The Stone

Now that the flood of activity from the implementation of Sarbanes-Oxley has settled, regulators, auditors and insurers are smoothing the rough spots that remain in financial reporting.

by Meg Green

Now that they have two years' experience complying with the Sarbanes-Oxley Act, many industry leaders want to improve the way companies report their financial information.

The landmark legislation, which was intended to improve accounting oversight for public companies and restore investor confidence in the wake of financial scandals including Enron, Tyco and WorldCom, went into effect in 2004. Many applaud the act for improving accounting standards, but say more should be done.

In November 2006, six large auditing firms proposed a new financial reporting method and called for other major changes. Meanwhile, Securities and Exchange Commission Chairman Christopher Cox said he's willing to scale back some of the more onerous demands of the act's Section 404—which requires that companies establish internal controls for monitoring financial reporting and then assess the success of those controls—for smaller companies that have said they find the provisions too burdensome.

The SEC and the board expected to propose guidance to help auditors and companies interpret Section 404 sometime in December 2006.

And, in its second year of implementation, the cost of complying with the act has dropped, according to one study.

"It's typical when any significant legislation is passed," said Bob MacDon-

ald, chief executive officer of Allianz Income Management Service and retired chairman and chief executive of Allianz Life Insurance Company of North America. "Initially, there is a huge impact, and there's a period where you make adjustments, make changes. The bottom line is that as difficult and cumbersome as Sarbanes-Oxley was in the beginning, it had a very positive impact on the quality and substance of the management of public companies and improved the quality of auditing. It's had a positive impact on the quality of information you can see as an investor.

"What we are seeing now is the normal process of adjusting and smoothing and polishing the stone to make it work better. It's just a part of smoothing out significant legislation," said MacDonald, who currently serves on the audit committees of two public companies.

The Expectation Gap

The six largest global audit firms in the insurance industry—ranked by insurance clients' net premiums written, according to A.M. Best Co.'s special report—are calling for major changes in the way audits are done. In addition to expected requests, such as standardizing global accounting, audit and enforcement standards, they'd like to reduce the liability that auditor firms face, implement forensic accounting procedures to help reduce the risk of fraud, and introduce a new

reporting model that's more driven by forward-looking information.

PricewaterhouseCoopers, Deloitte, Ernst & Young, KPMG, BDO International and Grant Thornton International released the joint proposal at a financial seminar in November. The proposal calls for several measures to strengthen financial reporting and auditing.

For instance, the executives call to complete the effort by the International Accounting Standards Board and the Financial Accounting Standards Board to harmonize the differences between international and U.S. accounting, and also develop a single global audit standard.

"There's a sovereign aspect to accounting announcements," said Bill Boyd, financial regulation manager of the National Association of Mutual Insurance Cos. "That may be more evident abroad than it is here. There may be some built-in differences in the processes behind the creation of accounting standards that cause convergence to be done slowly, and there's not a thing wrong with that. I think the whole

- The four largest auditing firms together audit about 75% of insurance companies.
- The six largest auditing firms are calling for changes in how companies present financial information.
- In the second year of Sarbanes-Oxley, compliance costs have dropped.

Key Points