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CEO and CFO Certifications of Financial Information

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INTRODUCTION

New certification requirements arrived at the corporate suite in the summer of 2002 in the form of a one-time SEC Order and the watershed Sarbanes-Oxley Act (SOA). CEOs and CFOs of public companies must personally certify to disclosure/internal controls and the material accuracy and completeness of their companies' financial statements. This commentary uses the phrase "material accuracy and completeness of the financial statements" to refer to the financial information covered under the SEC's CEO/CFO certification order and the three certifications of the Sarbanes-Oxley Act of 2002. Although we believe this is an accurate paraphrase that captures the scope and intent of the CEO/CFO certification requirements, readers should refer to the specific document for the precise wording of the covered items.[1]

Our commentary introduces the SEC Order as the predecessor to the SOA's triple-certification regime, and analyzes and contrasts the SOA certifications. We also identify and critique some rapidly evolving best practices and, where appropriate, offer suggestions on certification compliance. We then highlight some of the long-term impacts of the SOA certifications on both management and the accounting profession, and, last, we identify several areas for future research.

WHAT LED TO THE CHANGE IN FINANCIAL REPORTING REQUIREMENTS?

Probably more than any one single catalyst of the new certification requirements was the Congressional testimony of former Enron CEO Jeffrey Skilling. Testifying in front of the U.S. Senate Banking and Commerce Committee in 2002 about the reasons for Enron's sudden implosion, Mr. Skilling claimed to be totally ignorant about the details of Enron's accounting. In fact, when asked about certain accounting matters, his response was, in essence, "That's not my area of expertise. That's why we have a top CFO like Andrew Fastow and good auditors." In his testimony, Skilling maintained that detailed financial reporting and disclosure vigilance was not the proper domain of a CEO, but that of the brigade of Enron's accountants and lawyers.

This unconvincing response to financial reporting and disclosure responsibility quickly opened the door to vigorous probing by the Congress about Skilling's educational training. Although he acknowledged having an M.B.A. from Harvard, he argued that this pedigree gave him little or no

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[1] For example, the wording in the SEC certification order is "no covered report contained an untrue statement of a material fact as of the end of the period covered by such report … no report omitted to state a material fact necessary to make the statements in the covered report, in light of the circumstances under which they were made, not misleading as of the end of the period covered by such report."

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appreciation for accounting. Little did Skilling know at the time that his remarks would move Congress ever closer to including the mandatory CEO/CFO certification requirements in the SOA signed into law just five months later. Concurrently, ousted WorldCom CEO Bernie Ebbers undoubtedly furthered Congress' resolve by allegedly being totally unaware of his CFO's financial reporting wrong-doing.

Even if Enron and WorldCom were above reproach in regard to financial reporting and disclosure, CEOs in the past two decades were typically not individuals with strong accounting and finance backgrounds. Corporate boards placed more emphasis on CEOs "drumming up deals, customers and investors, and serving as the corporation's public face" (Hopkins 2002). As a result, CEOs came to the office with resumes heavy on sales and marketing experience, but light on accounting and finance. Not surprisingly, CEOs pushed more of their financial responsibility off of their plates and onto those of the company's CFO and Controller. Without Congressional intervention in the form of the SOA certifications, this slippery slope of CEO financial reporting abdication could have led to the further compromise of financial reporting and disclosure integrity, particularly in light of the fact that roughly 80 percent of financial statement fraud involves the company's CEO or CFO (Ceniceros 2003).

THE UNPRECEDENTED SEC CERTIFICATION ORDER

On June 27, 2002, in the wake of the Enron disaster and initial revelations by WorldCom that its earnings, equity, and assets had been overstated by several billion dollars, the SEC issued a one-time, retrospective order requiring CEOs and CFOs of the largest U.S.-based public companies, with revenues over $1.2 billion, to personally and separately file sworn statements regarding the material accuracy and completeness of their companies' most recent periodic reports. The certifying officers were required to file their personal statements individually with the SEC no later than the close of business on August 14, 2002, or the first day thereafter that their companies were required to file a Form 10-K or Form 10-Q with the SEC. Of the 947 large companies affected, 691 faced a deadline of August 14.

The certification order had retroactive implications as it applied not only to the most recent fiscal year, but to all 10-Qs, 8-Ks, and proxy materials filed since the last 10-K (SEC 2002a, 2002b). As an additional investor safeguard, the certification required each CEO and CFO to declare whether the contents of the statements were reviewed with the company's audit committee, or in the absence of an audit committee, the independent members of the company's board of directors. Embracing transparency for America's investors, the SEC announced that it would make all the certifications available to the public on the SEC website. Although the SEC certification order was silent on sanctions and penalties, the follow-up SEC press release warned that officers who make false certifications will face personal liability. As for those officers who did not file certifications at all, the SEC warned that they risk removal from office or prosecution by the Justice Department (Williams 2002a).

Prior to the SEC certification order, senior corporate officials often did not sign every filing with the SEC; when they did it was on behalf of the company and not as a personal endorsement. Because the new order required senior executives to swear in writing that to the "best of my knowledge" the periodic reports were materially accurate and complete, on the eve of the deadline, some companies quietly made inquiries to the SEC to see if they could couch or modify their sworn statements by adding words, footnotes, or explanations. In a clear and determined response, an SEC spokesperson stated that "this is black or white, there is no gray" (Beckett and Talley 2002). A prominent securities lawyer warned that those companies that tried to do such an end run around the certification would be exposed on the SEC's website as having officers unable to give a "clean certification" (Beckett and Talley 2002).

Critique of Best Practices in Action: Summer 2002

I. T. Battenberg III, CEO of Delphi Corp., was the first CEO of the targeted companies to certify that his company's periodic reports were materially accurate and complete. Significantly, he executed his personal attestation a month before the deadline. Before signing his certification, Battenberg implemented a vigorous and robust vetting process, all toward educating himself about the information contained in the periodic reports. As a result, for the first time as a CEO he attended the board of directors' audit committee meetings (Grimsley 2002). Conferring privately with Delphi's outside auditors, Battenberg asked them to meet with all of Delphi's senior executives for a "no-holds-barred" interchange. He also made sure that all his division heads had the same kind of constructive engagement with the external auditors, and, after he completed his own review, he certified the periodic reports with the SEC.

FedEx, Corning, and EDS Corp. were among 16 companies whose CEOs and CFOs provided the required certifications weeks before the deadline. A company that has long valued financial transparency and maintained tight financial controls, FedEx found itself in the middle of replacing its old independent auditor, Arthur Andersen LLP, with Ernst & Young LLP when the certification order first appeared. One permanent change in internal reporting controls required, for the first time, that the chief executive of each subsidiary was required to sign off on their results. Previously, that requirement only applied to CFOs of FedEx's half-dozen business units. To FedEx's CFO, expanding the list of internal signatories added one more set of eyes to the accuracy and completeness of the company's public disclosures (Perez 2002).

Several other CEOs mandated verification of periodic reports down through the corporate chain of command before they personally signed off. DuPont Co. had the most subordinate certifications, requiring more than 80 business executives and vice presidents to sign a form verifying the accuracy of the company's results. Boise Cascade Corp. followed closely with 68 lower-level executive verifications, but, commendably, the company implemented this internal certification requirement decades ago (Perez 2002).

The CEO of Harrah's Entertainment, Inc. added personal interviews of division heads to his subordinate certification regime. Every division manager had to sign a letter attesting to the accuracy and completeness of their respective numbers and was subjected to vigorous cross-examination by the CEO (Williams 2002b). Additionally, the resourceful CEO created a kind of "informant network," where any employee could anonymously report a problem—accounting or otherwise—to an outside firm that independently investigated the claim and reported its finding directly to the board's audit committee. By engaging in such aggressive and prudent self-policing, a company later found guilty of a crime could reduce fines by up to 95 percent under the 1991 federal sentencing guidelines (Seidenberg 2002).

In contrast, Office Depot, Inc.'s multiyear string of disappointing financial results had earlier prompted its CEO to become intimately involved with the company's financial reports. The fact that he did not delegate the certification order to subordinates is instructive from a best practices standpoint. Though the SEC Order encouraged meetings with top financial officers, he "didn't even consider" asking subordinate executives to sign internal attestations (Perez 2002). Such a move, the CEO argued, could be perceived as the CEO and CFO conveniently abdicating their financial reporting and disclosure responsibilities to subordinates.

A best practices suggestion from the securities bar was for CEOs to keep formal records of their inquiries into their companies' financial condition as "proof" that they had asked the right questions of the right people (Williams 2002b).

August 14 Deadline

When the August 14 certification deadline arrived, there were no large-scale restatements, and no CEO resignations. CEOs and CFOs of 16 companies did not certify to the accuracy and completeness of their companies' financial reports and instead filed explanations or other forms of certification.

Several apparently excusable reasons, like continuing internal or SEC accounting investigations, awaiting audited restatements, newly appointed CEOs or auditors, were offered by the 16 delinquent companies.

In less than 50 days, without any real substantive guidance from the SEC, the CEOs and CFOs of nearly 700 companies scrambled to comply with the August 14 certification deadline, with nearly 250 more companies needing to comply with the SEC Order by December. These senior officers would have an advantage on the more complex and comprehensive certifications later mandated by the SOA.

THE SARBANES-OXLEY ACT'S TRIPLE CERTIFICATIONS REQUIREMENT

The SOA created three new separate and distinct certifications that are legally and substantively different in terms of what they require. Notwithstanding some guidance from the SEC, ambiguity and confusion still exist regarding certification procedure and scope. Consequently, CEOs and CFOs must study and fully comprehend these evolving certification requirements.

Coupled with SEC final rules implementation, the SOA inaugurates a triple-certification regime consisting of:

1. Section 302—CEO/CFO annual and quarterly report assurances, internal control assurances for financial reporting; "disclosure controls and procedures" assurances; and disclosure to the audit committee and external auditors of material weaknesses in internal controls and fraud.
2. Section 404—CEO/CFO assessment of "internal control over financial reporting" in the form of an internal control report filed with each annual report and a separate requirement that external and independent auditors issue an attestation report on management's assessment of the internal controls.
3. Section 906—CEO/CFO annual and quarterly periodic report assurances, that trigger severe criminal penalties from the Department of Justice for false certifications.

Under the Sarbanes-Oxley Act, CEOs and CFOs have a continuous and active duty to remain informed about their companies' financial affairs. Although CEOs and CFOs can and should solicit input from lower levels of management, they retain primary responsibility for the ultimate certifications. In the sobering words of an SEC Commissioner, the SOA certification regime requires that the CEO and board of directors maintain procedures to ensure that they "hear bad news," and all material financial and nonfinancial information, for the benefit of the investing public (Glassman 2002). Lamentably, a recent survey reveals that nearly one-third of the surveyed public companies report that their CEOs did not participate in the review of periodic earnings report information prior to its release (*Newswire* 2003). This revelation underscores the need for CEOs to take the SOA certifications seriously and not delegate primary responsibility for their company's financial information.

Section 302 Certification: CEOs and CFOs Bear Responsibility for Information Flows

Compared with the SEC certification order that targeted the nation's largest public companies, Section 302 goes well beyond the SEC order in two material respects. First, Section 302 targets all 15,000 companies whose securities are publicly traded, including more than 1,300 companies based outside the U.S. To comply with Congressional language in Section 302, the final SEC rules require certifications from all public companies required to file periodic reports. Second, Section 302 is permanent and applies going forward, whereas the SEC Order was a one-time, retrospective requirement.

"Internal Control over Financial Reporting" and "Disclosure Controls and Procedures"

The SEC's final rules augment Section 302 with two new terms: "internal control over financial reporting" and "disclosure controls and procedures" (SEC 2003). The SEC made clear that its

definition of "internal control over financial reporting" is part of the "common definition" of the COSO (Committee of Sponsoring Organizations of the Treadway Commission) study of internal control. However, the SEC acknowledges that its definition only "encompasses the subset of internal controls" addressed in the COSO Report that pertains to broader financial reporting objectives (SEC 2003). The SEC definition:

> does not encompass the elements of the COSO Report definition that relate to effectiveness and efficiency of a company's operations and a company's compliance with applicable laws and regulations, with the exception of compliance with the applicable laws and regulations directly related to the preparation of financial statements, such as the Commission's financial reporting requirements. (SEC 2003)

Not surprisingly, this definition is consistent with the description of internal accounting controls in the Securities Exchange Act Section 13(b)(2)(B). Most significantly, the SEC explicitly includes the safeguarding of company assets in its definition of "internal control over financial reporting" (SEC 2003), which is consistent with the COSO Report addendum and the primary objectives of internal accounting controls in Statement on Auditing Standards (SAS) Nos. 55 and 78 (AICPA 1988, 1995).

The Securities Exchange Act Rule 13a-15(d) defines the term "disclosure controls and procedures." The SEC recognizes that while there is substantial overlap between the definitions of "internal control over financial reporting" and "disclosure controls and procedures," many companies will design their "disclosure controls and procedures" so that they do not cover all components of "internal control over financial reporting" (SEC 2003). The SEC wants companies to exercise their best judgment and have some flexibility in developing the process that they will rely on to meet applicable requirements. As an example, the SEC cites dual signature requirements or limitations on signature authority of checks as a component of safeguarding company assets. Companies nonetheless would still be in compliance with Section 302 if they determined that this control procedure is not part of "disclosure controls and procedures."

The Section 302 controls and procedures are designed to ensure that information is accumulated and communicated to the company's management, including its CEO and CFO, for them to make timely decisions regarding required disclosures. Since the SEC adopted final rules that require management to certify their maintenance and evaluation of both internal and disclosure controls, this certification may become quite costly to companies in terms of labor and time (SEC 2003). Regardless of cost, Section 302 appears to impose a duty of investigation on the part of CEOs and CFOs (Brockett 2002).

Although Congress did not identify Form 8-K and other such current reports as being subject to Section 302, the final SEC rules provide that the new "disclosure controls and procedure system" applies to the full and timely disclosure in current reports. However, there is no specific certification requirement relating to current event reports on those forms (SEC 2002c).

Adherence to GAAP Not Enough

The "best of knowledge" certification requirement regarding fair presentation of financial statements and other financial information must meet a standard of overall material accuracy and completeness that is broader than financial reporting requirements under GAAP (SEC 2002c). Section 302 specifically states that application of GAAP alone may not fulfill the intent of presenting a materially accurate and complete portrayal of the company's financial results. In the SEC's view, Section 302 requires that companies properly apply not only acceptable, but also *appropriate* accounting procedures. Moreover, they must disclose financial information that is informative and that reasonably reflects the underlying transactions and events, and provide any additional disclosure necessary for investors to have a materially accurate and complete picture of a company's financial

condition, results of operations, and cash flows. CEOs and CFOs not only need to be accounting savvy, but they must also be aware of the subtle warning that adherence to GAAP alone may not satisfy this threshold of financial disclosure. Section 302 therefore applies a supra-GAAP requirement on financial information under the purview of the CEO and CFO. Since the certifications apply not only to the financial statements, but also to all public disclosures, and because the SEC historically has looked very carefully at MD&A (SEC 1989), senior management should pay particular attention to their analyses and forward-looking discussions in their MD&A disclosures.

Certification Procedures

Similar to the one-time SEC Certification Order, the SEC did not prescribe any particular procedures for conducting the required review and evaluation under Section 302. Instead, it expects each company to develop a process that is consistent with its business and internal management and supervisory practices. Companies must find their own best practices through trial and error. Nevertheless, the SEC exhorts companies to create a committee to report to senior management, including the CEO and CFO, charged with the responsibility for considering the materiality of information and determining disclosure obligations on a timely basis.

Although the SEC only recommends, but does not mandate, the creation of a "disclosure committee," failure to have such a committee may identify a potential control weakness to plaintiffs alleging injury from false and misleading financial disclosures (Wardwell and Surdykowski 2002). The SEC expects this committee to bear the responsibility for considering the materiality of information and determining disclosure obligations on a timely basis (SEC 2002c). Additionally, the SEC suggests that the committee include the principal accounting officer (or the controller), the general counsel, the principal risk management officer, the chief investor relations officer, and other officers or employees, including those associated with individual business units, as the company deems appropriate (SEC 2002c). We suggest that a credit expert also be considered for such a committee, particularly in light of the new policy by the largest credit-rating agencies to include evaluations of accounting practices and policies in their creditworthiness reports. Credit agencies might have more confidence in a company that has a credit expert participate in monitoring disclosures.

Form of Certifications

Section 302 certifications are in addition to, and thus do not alter, the current signature requirements for quarterly and annual reports filed under the Securities Exchange Act. Consequently, the SEC clearly stated that an officer providing a false Section 302 certification potentially could be subject to both SEC civil action and private shareholder action for violating federal securities laws (SEC 2002c). Section 302 requires CEOs/CFOs to certify that they disclosed to the company's audit committee and external auditors any material weaknesses in internal controls and procedures that could adversely affect financial reporting, and publicly report any fraud that involves management or internal controls employees.

Previous instructions for quarterly reports on Form 10-Q required the report to be signed on the company's behalf by a duly authorized officer of the company, not necessarily the CEO, and the CFO or chief accounting officer (Schwartz and Freedman 2002). Although the CEO need not sign the quarterly report under the SOA, the CEO must provide the Section 302 certifications as exhibits to the periodic reports to which they relate. Separate certifications by each certifying officer must be included in the applicable report immediately following the signature section of these reports (Best and Blair 2002).

The Pros and Cons of Subordinate Certifications under Section 302

The SEC Certification Order led many companies to document or consider documenting compliance that also applies to Section 302 disclosure controls and procedures by requiring subordinates to execute internal certifications. The SEC neither encourages nor discourages internal certifications.

Although this type of "360-degree" certification policy could alert others to the paramount importance of accurate and reliable information in the company's SEC filings, we note earlier that such down-the-line certifications do not substitute for the activist due diligence duty that Section 302 requires of CEOs and CFOs.

Notwithstanding the obvious utility of internal certifications, the securities bar underscores at least one caveat about their usage. Because some junior-level managers and executives will balk at executing these certifications, CEOs and CFOs must evaluate the effect subordinate certifications could have on officer morale, corporate culture, and the practical ability to delegate responsibility appropriately among such officers (Vinson and Elkins LLP 2002). As for the practical risk that an officer refuses to provide such a certification, the CEO and CFO must determine whether this refusal is the result of a lack of cooperation or a red flag indicating that a substantive problem exists.

Seemingly leading the way on Section 302 best practices are Coca-Cola and Tenneco Automotive. For example, Coca-Cola expanded its existing annual processes to be applied each quarter. Formal written certification is required quarterly from each operating unit's president, CFO, legal counsel, and the heads of the company's global function. Modeled after the external auditor representation letter, Coca-Cola adds elements from the CEO/CFO certification to operating management's duty to identify business trends and developments. The controller's office analyzes all the letters and highlights items crucial to Coca-Cola's disclosure committee. Tenneco codified its disclosure controls and procedures in a detailed, step-by-step manual, and its disclosure committee meets at least three times prior to filing the 10-Q (Graziano 2002).

SECTION 404 CERTIFICATIONS: MANAGEMENT'S INTERNAL CONTROL REPORT AND EXTERNAL AUDITOR'S ATTESTATION

On June 5, 2003, the SEC adopted final rules that implement the Section 404 certifications under the SOA (SEC 2003). Large public companies with fiscal years ending on or after June 15, 2004, will be among the first public companies to comply with Section 404. Although the statutory focus of this section is on the integrity and transparency of all periodic reports, it also incorporates special requirements for annual reports. All annual reports of public companies, except investment companies, must therefore contain an "internal control report" wherein management affirms its responsibility for maintaining an adequate system of internal control and assesses the effectiveness of the system.

Despite the SEC's attempts at clearing up the ambiguity of the new term "internal control over financial reporting," practitioners disagree over whether the SEC's definition mirrors the AICPA's Codification of Statements on Auditing Standards (AU) Section 319, *Consideration of Internal Control in a Financial Statement Audit* (AICPA 2002). We believe that in order to be consistent with the fiscal accountability and transparency spirit of SOA, the construct of "financial reporting" extends to MD&A, press releases, and all references to financial performance metrics.

Internal control is a process designed primarily to provide reasonable assurance about the safeguarding of assets and the reliability and completeness of financial information. It includes a system of established procedures and policies to capture financial information as well as deter, detect, and report abuses, accounting errors, and fraud. The SEC's application rules require companies to perform *quarterly* evaluations of changes that materially affected or are reasonably likely to materially affect the company's internal control structure over financial reporting.

Content of Management's Control Report

As to the content of management's annual internal control report, it must identify the "framework" used by management to evaluate the effectiveness of internal controls, and affirm that the external auditor issued an attestation report affirming management's assertions (SEC 2003). In its final rules, the SEC states that companies may use the COSO framework as an evaluation framework

since it was subject to an open "due process" during its creation. The internal control report must also disclose any material weakness in internal control and, importantly, management cannot conclude that the company's "internal control over financial reporting" is effective when there are one or more material weaknesses (SEC 2003).

Section 404 not only directly impacts management, it also expands the external auditor's responsibilities by effectively requiring each registered public accounting firm that audits a public company to attest to and report on management's assessment of the company's internal controls and procedures for financial reporting (SEC 2002). The company must reference the auditor's attestation and include both it and their internal control report as exhibits to its annual report (SEC 2003). The auditor's attestation must be made in accordance with standards established by the newly created Public Company Accounting Oversight Board (PCAOB), charged by the SEC to adopt standards governing all public company audits (SOA, U.S. House of Representatives 2002). However, as of this writing the PCAOB has not provided guidance to auditors in their attestation on company controls. This delay in promulgating guidance was one of the stated reasons the SEC deferred the effective date of Section 404 until 2004 at the earliest.

Although the Securities Exchange Act Section 13(b)(2)(B) already requires internal controls for public companies, Section 404 adds a new requirement of written attestation. Implementing this certification requirement, including the additional control testing necessary for companies and external auditors to support their assertions and attestations, may make this item the most costly under SOA to execute.

SECTION 906 CERTIFICATION: JAIL TIME FOR CEOS AND CFOS WHO FALSELY CERTIFY PERIODIC REPORTS

Unlike the Section 302 and 404 certifications, the Section 906 criminal certification took immediate effect upon enactment of the SOA, with final rules effective August 14, 2003 (SEC 2003). Although Section 906 differs substantively from the Section 404 certifications, at first blush it appears similar to Section 302. However, among the more controversial aspects of the SOA is the confusing interplay between Sections 302 and 906. Fundamentally, each periodic financial report filed at the SEC is subject to two separate certifications:

- the one pursuant to Section 302 that is filed as an exhibit to the periodic report, and
- the one pursuant to Section 906 that will not be filed as part of the periodic report, but "furnished" with each report as an exhibit (SEC 2003).

Section 906 requires CEOs and CFOs of public companies to certify to the completeness and accuracy of the periodic quarterly and annual reports containing financial statements filed with the SEC. Specifically, CEOs and CFOs must certify both that the content of the periodic report "fully complies" with the Securities Exchange Act's applicable reporting requirements and that the information contained in the report "fairly presents," in all material respects, the financial condition and results of operations of the company. Although this sounds similar to the Section 302 certifications, the Section 906 certification adds a new due diligence layer by requiring CEOs and CFOs to certify that the report "fully complies" with the requirements of the Securities Exchange Act (SOA 2002; Fisher and Karpf 2003). Because Section 906 amends the U.S. Criminal Code and is within the jurisdiction of the Justice Department, and what "fully complies" actually entails has not yet been clarified by the SEC, CEOs and CFOs are potentially at risk. What is clear, however, is that the "fairly presents" provision in Section 906 requires a broader certification than the typical external auditor's attestation on the financial statements.

Section 906 imposes severe criminal penalties for false certifications made knowingly or willfully. Unfortunately, Section 906 does not explore the difference between a "knowing" violation (up to $1 million fine and/or 10 years in prison) and "willfully" committing a "knowing" violation (up to

$5 million fine and/or 20 years in prison). But it is clear that Section 906 dramatically increases CEO/CFO exposure to criminal prosecution by the Justice Department when they are not personally and substantively involved in monitoring and correcting financial misconduct and reporting to the public (Urgenson et al. 2002). Finally, unlike Section 302, Section 906 certifications may take the form of a single statement signed by a company's CEO and CFO (SEC 2003).

The need to comply with Section 906 certifications will undoubtedly increase the risk of criminal prosecution for CEOs and CFOs involved in a restatement of past results filed in periodic reports. This is especially true with respect to CEOs certifications of quarterly financial results, since CEOs, unlike CFOs, previously were not required to sign Forms 10-Q. If executives are the targets of Section 906, then it is likely that greater pressure from the Justice Department to settle should elicit increased guilty pleas by executives.

Table 1 compares and contrasts the salient points in Sections 302 and 906.

HOW THE CERTIFICATION REGIME AFFECTS MANAGEMENT'S RELATIONSHIPS, ROLES, AND FUNCTIONS

The emergent financial certification era will require CEOs to forge new and stronger relationships with other corporate executives. As partners in certification, CEOs and CFOs must forge stronger and more interactive working relationships. CFOs will need to help arm CEOs with accounting acumen. The negative to this is that in 2002 only 20 percent of all *Fortune* 500 CFOs were CPAs (Scarinci 2003); presumably a substantial number of CFOs will also need to increase their detailed financial reporting and internal control expertise.

TABLE 1
Comparison of Salient Features of Section 302 and 906 Certifications

Feature	Section 302	Section 906
Effective date	August 29, 2002 (August 14, 2003 for final rules)	July 30, 2002 (August 14, 2003 for final rules)
Form of Certification	Separate certification by CEO and CFO	May take the form of a single statement signed by the CEO and CFO
Reports Covered	Annual and Quarterly Reports	Annual and Quarterly Reports
Scope of Certification	- financial information is materially accurate and complete - maintaining disclosure controls and procedures - adequacy of internal control over financial reporting	- Periodic reports "fully comply" with the Securities Exchange Act - Financial information in the periodic reports "fairly presents" in all material respects
Adherence to GAAP	Supra-GAAP	Subject to pending Department of Justice interpretation
Disclosure Control Committee	Recommended by SEC	Subject to pending Department of Justice interpretation
Audit committee communications with external auditor	CEOs/CFOs must disclose material weaknesses in internal control	Subject to pending Department of Justice interpretation
How certifications delivered	Filed as an "exhibit" to each periodic report	"Furnished" as an exhibit to each periodic report
Enforcement Jurisdiction	SEC	Department of Justice
Penalties for false certifications	SEC civil action	Department of Justice criminal prosecution

Although the certification mandates do not require companies to designate a risk management officer, the time may come for corporate America to place the chief risk officer (CRO) on a permanent rung on the organizational ladder. Companies might include a "risk factor" section within the annual report on Form 10-K (Wardwell and Surdykowski 2002), or the CEO may again embrace the role of a corporate ethics officer. In fact, within a few months of the enactment of the SOA, some 100 companies hired newly appointed ethics officers (Swartz 2003).

CIA-type background investigations may become more commonplace when recruiting new CEOs/CFOs. Companies will probably be more interested in individuals who follow the "spirit as well as the letter" of the new certification regime (Ceniceros 2003). Moreover, companies will begin to more heavily target CEOs who are GAAP-sensitive and accountant-friendly.

Last, additional formal education may be needed to enhance deterrence and compliance. To equip themselves, many CEOs may either audit or take courses in financial accounting and controls; CFOs could study forensic accounting. On the national level, an SEC academy of corporate responsibility and integrity might emerge to train CEOs and CFOs on financial reporting and disclosure issues as well as the nuances of SOA certifications (Taylor 2002).

THE IMPACT OF THE CERTIFICATION REGIME ON THE ACCOUNTING PROFESSION

We foresee several long-term, positive impacts on the accounting profession. First, since the PCAOB has not yet adopted the rules and standards that will guide external auditors in their internal control attestations, the accounting profession is uniquely positioned to have some input into this process. Given the current political tension between the PCAOB and the AICPA, any overture of assistance from the AICPA must be approached with great diplomacy. Additionally, accounting and auditing academics, particularly through current efforts in the American Accounting Association's Auditing Section, may have an unprecedented opportunity to assist the PCAOB in developing these standards for public audits.

Second, because of their broad financial reporting and internal control knowledge, accounting academics may find some new opportunities to join corporate boards. Because CEOs and CFOs will need to work more closely with the audit committee of the board of directors in the new certification regime, more companies are seeing the benefits of adding an "audit committee financial expert" to their audit committee. Several stock exchanges proposed that audit committees contain at least one financial expert. As a result, the stature of the accounting academic could rise commensurately if these individuals have the opportunity to serve on boards and committees of public companies.

Third, the new requirement of the external auditors' attestation report on internal control will not only increase hiring in the public accounting profession to do this additional work, but it will also provide additional revenue resources to public accounting firms that were restricted by other provisions of SOA, particularly in providing "consulting" and "internal control outsourcing" services. More importantly, the new focus on internal control should help restore public confidence in both the financial reporting system and independent audits in the U.S. This restoration of confidence should enable the accounting profession to distance itself from much of the lingering fallout from the Enron era.

Fourth, preemptive and investigatory forensic accounting may become a new risk management approach in companies. There should be increased demand for forensic accountants and such positions may appear on corporate organization charts. Internal and external accountants may find that a transfer to such a position is a career enhancing move.

Finally, the information technology (IT) auditor will become a key advisor to the director of internal audit, upper management, and the audit committee (Messmer 2003). IT auditing and information security are crucial in implementing, evaluating, and documenting the internal controls mandated by the SOA. Consequently, the IT auditing field will likely continue to expand and create new career niches for accountants.

AREAS FOR FUTURE RESEARCH

Several interesting areas for research surface as a result of the SEC certification order and the SOA's triple-certification requirements. While our discussion is not exhaustive, it is intended to identify several issues that will benefit from further academic investigation. These include:

- What are the effects of CEOs requiring subordinate certification of financial results on psychological factors like job satisfaction, morale, budget-setting behavior, turnover, and perceptions of operational and business risk?
- Do companies hire different types of individuals into CEO, CFO, or board positions after SOA?
- What are the profiles of companies and individuals prosecuted under the SOA?
- Do prosecutors seek relief under Section 302 or Section 906 for certification overlaps?
- Do companies use their external auditor or another audit firm in evaluating the adequacy of their internal controls?
- What constitutes a "material weakness" in internal control that gets reported to the public?
- What types of other information are communicated in auditor and management reports on internal control?
- Have companies improved their systems of internal control, financial disclosures, or accounting methods due to the passage of SOA?
- Do users of the financial statements believe that there has been any significant improvement in the reliability of the financial statements or disclosures due to CEO/CFO personal certifications or heightened emphasis on internal control?
- Has the PCAOB's standard-setting process been effective?

CONCLUSIONS

The financial reporting theme of this commentary emphasizes that the one-time SEC Order and the SOA triple-certification regime forced CEOs, and many CFOs, to become much more sensitive and knowledgeable about financial reporting and required disclosures, and to re-evaluate their systems of internal control. Gone forever are cavalier CEO attitudes that protest that they need not know much regarding financial accounting and reporting. At the heart of this series of certification requirements is CEO/CFO personal oversight and responsibility for the content and quality of financial information, and increased involvement with internal control. Although these new requirements have the ability to significantly improve financial reporting and disclosure, only long-run adherence to the spirit as well as the letter of the requirements will effectively increase the actual level of reporting accuracy and transparency of public companies in the U.S.

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