

APPENDIX C – CURRENT GOVERNANCE SYSTEM

OVERVIEW AND HISTORICAL PERSPECTIVE

1 Society often grants professions the right to regulate themselves to protect the interests of both their members and the public. The auditing profession has long maintained a voluntary, self-regulatory governance system through the activities of the American Institute of Certified Public Accountants (AICPA)¹ and, in more recent years, the Financial Accounting Standards Board (FASB), Independence Standards Board (ISB), SEC Practice Section (SECPS) and Public Oversight Board (POB). This system has been improved and modified continually as political, social and economic conditions and needs have changed.

2 Although the goals of self-regulation and public regulation are similar – protecting the public interest – and the two systems operate in concert with one another, there are important differences. Robert K. Mautz noted that:

Public regulation is conducted with the full power of the state in support of established requirements. Self-regulation has no equivalent authority. At most, it can exclude noncomplying members from whatever benefits group membership confers or impose whatever sanctions members have voluntarily agreed to accept. Such powers as the ability to subpoena records and witnesses are not available in self-regulation.²

3 In the mid-1970s, reports of U.S. companies paying bribes to foreign officials and several highly publicized corporate bankruptcies resulted in the U.S. Congress looking into the accounting profession. Hearings were held in both the House of Representatives (chaired by John E. Moss) and the Senate (chaired by Lee Metcalf) to investigate these matters and the role of independent auditors. In 1977, the profession created the SEC Practice Section as part of the Division for CPA Firms of the AICPA, which gave rise to unprecedented voluntary self-regulatory initiatives:

- Independent oversight of the SECPS by the POB
- Mandatory peer review
- Mandatory continuing professional education
- Establishment of the Quality Control Inquiry Committee (QCIC) (initially called the Special Investigations Committee)

¹ Including the Auditing Standards Board (ASB) (see Appendix A).

² Robert K. Mautz, “Self-Regulation: Perils and Problems,” *Journal of Accountancy* (May 1983) (initially presented as an address at the AICPA’s tenth national conference on current SEC developments [January 1983]).

These initiatives required SECPS member firms to subject their professional practices to peer review, independent oversight by the POB and scrutiny by the SEC.

4 Initially, membership in the SECPS was voluntary. Membership grew rapidly in the initial three years to include CPA firms that audited approximately 75% of all SEC registrants. There was criticism, however, of the voluntary nature of participation and the fact that non-participating CPA firms that audited SEC registrants numbered in the hundreds. In response, in 1988, the AICPA membership changed its by-laws to mandate that each individual member of the AICPA who provides attest services to an SEC client (as defined in the SECPS membership requirements) be employed by or affiliated with a CPA firm that is an SECPS member.³ Presently, there are approximately 1,300 member firms in the SECPS that collectively audit more than 99% of all U.S.-based SEC registrants.

5 The SECPS created a structure and requirements for its member firms with one end in mind – to protect the public interest by improving the quality of practice by CPA firms before the SEC. Each member firm is required to install a system of quality control to provide reasonable assurance that the firm conforms with professional standards in conducting its accounting and auditing practice. The requirements are flexible enough to allow firms of all sizes (from sole practitioners to international firms) to design and operate systems that are appropriate for their practice. The system of quality control must include elements related to independence, integrity and objectivity; personnel management; acceptance and continuance of clients and engagements; engagement performance; and monitoring.

THE COMPONENTS OF SELF-REGULATION

6 The profession's self-regulatory system complements public regulation. Self-regulation extends beyond public regulation in some areas (discipline, for example), while in other areas, such as standard setting, it largely takes the place of public regulation. The profession's self-regulatory structure includes bodies that set professional standards as well as bodies that conduct the related compliance and disciplinary procedures that apply to CPAs and CPA firms as a result of their voluntary memberships in the AICPA. The standards include technical, ethical and quality control standards, and requirements for continuing professional education. A chart of the current governance structure is included in Table 1 at the end of this appendix.

Public Oversight Board

7 At the time of its formation, the SECPS sought to quiet those who might question the effectiveness of a voluntary self-regulatory model whose cornerstone would be a review by, and among, peers. Although a public regulatory system was already in place, the SECPS wanted an independent component that would represent the public interest. This led to the POB.

³ Non-compliance by an individual AICPA member results in his or her expulsion from the AICPA.

8 The POB comprises five independent public members – primarily non-accountants with a broad spectrum of business, professional, regulatory and legislative experience – who represent the public interest. The POB nominates and elects its own replacements. The current members are:

- Charles A. Bowsher, Chairman, Comptroller General of the United States and head of the General Accounting Office (1981–1996), Partner of Arthur Andersen & Co. (1971–1981), Assistant Secretary of the Navy—Financial Management (1967–1971) and corporate director
- Donald J. Kirk, Vice Chairman, Financial Accounting Standards Board, member (1973–1977) and Chairman (1978–1986), Partner of Price Waterhouse & Co. (1967–1973), Columbia Business School, Professor (1987–1994), Executive-in-Residence (1995–present) and corporate director
- Melvin R. Laird, Secretary of Defense (1969–1973), Counselor to the President (1973–1974), nine-term member of the U.S. House of Representatives (1953–1969)
- Norman R. Augustine, Chairman and CEO of Martin Marietta Corporation (1987–1995), Chairman and CEO of Lockheed Martin Corporation (1996–1997), Assistant (1973–1975) and Under (1975–1977) Secretary of the Army, Chairman and Principal Officer of the American Red Cross (1992–present) and corporate director
- Paul H. O’Neill, Chairman and CEO of Alcoa (1987–1999) and corporate director

9 The POB has sole discretion in the hiring and replacement of its Executive Director, who is responsible for hiring and supervising the technical and administrative staffs. Dues paid by SECPS member firms support the POB; however, the POB is responsible for determining all aspects of its budget, including compensation levels of the Board members and the staff.

10 The POB’s primary function is to monitor and report on the activities of the SECPS. Its objective is to safeguard, and act as an advocate of, the public interest. Accordingly, the POB meets regularly with standard-setting bodies, public regulators and those responsible for the various SECPS activities.

11 Over the years the POB has expanded its role by identifying and commenting on issues related to the quality of auditing and financial reporting in the United States. In that capacity, the POB has issued reports that include:

- *Scope of Services by CPA Firms* (1979), an analysis of and recommendations

regarding non-audit services provided by CPA firms to their SEC audit clients

- *Public Perceptions of Management Advisory Services Performed by CPA Firms for Audit Clients* (1986), a research report prepared by the Survey Division, Audits & Surveys, Inc., which reported the survey results of nine key publics' perceptions of the management advisory services (MAS) issue. The survey results suggested that members of the key publics think that performing certain MAS can impair objectivity and independence and that caution needs to be exercised when CPAs perform any MAS for their audit clients.
- *In the Public Interest* (1993), a special report dealing with issues confronting the accounting profession
- *Strengthening the Professionalism of the Independent Auditor* (1994), by the Advisory Panel on Auditor Independence, chaired by Donald J. Kirk and often referred to as the Kirk Panel Report. The Advisory Panel was formed in response to concerns expressed by the Chief Accountant of the SEC in January 1994 regarding his perceptions of auditors' acquiescence to clients' accounting policies. The recommendations in the report called for auditors to look to the audit committee and the board of directors – the shareholders' representatives – as the audit client, not corporate management.
- *Allies in Protecting Shareholder Interests* (1994), a report to directors, management and auditors that discusses the corporate governance recommendations contained in the Kirk Panel Report

SEC Practice Section

12 The SECPS's activities are carried out by its Executive Committee, Peer Review Committee, QCIC, SEC Regulations Committee, and the Professional Issues Task Force (PITF).

SECPS Executive Committee

13 The SECPS Executive Committee governs the SECPS's activities, which are subject to oversight and public reporting by the POB. The responsibilities of the SECPS Executive Committee include:

- Establishing the SECPS membership requirements
- Establishing budgets and dues requirements to fund the SECPS's activities
- Determining sanctions to be imposed on member firms for failing to comply with the SECPS membership requirements
- Appointing persons to serve on such committees and task forces as are necessary

to carry out the SECPS Executive Committee's functions

- Consulting from time to time with the POB

14 Well-defined membership requirements are critical to the SECPS's overall success. The SECPS adopted numerous membership requirements at the outset, and has continued to amend and add to them as times and circumstances have changed. The principal membership requirements include:

- Adhering to quality control standards established by the AICPA
- Submitting to a peer review of the firm's accounting and auditing practice every three years
- Ensuring that all professionals within the firm participate in specified amounts of continuing professional education
- Assigning an audit partner to be in charge of each SEC engagement up to a maximum of seven years
- Assigning a second partner to perform a preissuance concurring review of the auditor's report and financial statements of each SEC client
- Establishing independence policies covering relationships between (a) the member firm, its benefit plans and its professionals (and the close relatives of such professionals) and (b) "restricted entities" of the firm (i.e., all audit clients that are SEC registrants and certain entities related to such clients)
- Maintaining an independence database that includes, at a minimum, (a) all restricted entities and (b) for firms with at least 7,500 professionals, partners' and managers' investment holdings, so the two can be matched on a timely basis
- Designating a senior-level partner to be responsible for timely updates to the independence database and for overseeing the adequate functioning of the firm's independence policies and consultation process
- Seeking adoption of policies and procedures by a firm's international organizations or individual foreign associated firms whereby (a) a "filing reviewer" (a person or persons knowledgeable in accounting, auditing and independence standards generally accepted in the United States) would perform certain limited review procedures prior to the submission of certain SEC filings that include or incorporate the foreign associated firm's audit report, and (b) a sample of SEC audit engagements would be reviewed as part of the annual inspection program of the international organization or the individual foreign associated firms
- Reporting annually the names and countries of the foreign associated firms that have represented that they have established such policies and procedures
- Filing with the SECPS each year an annual report containing certain demographic and statistical data related to the firm's attest, tax and MAS services to SEC clients
- Reporting annually to the audit committee or board of directors of each SEC client on the total fees received from the client for MAS and a description of the services
- Reporting to QCIC within 30 days of being served with any litigation or regulatory proceeding relating to alleged audit deficiencies in the audit of an SEC client

Peer Review Committee

15 CPA firms are required to create a system of quality control, in accordance with promulgated standards, that is appropriate for their size, the nature and complexity of their practice, and other factors. The peer review process was established to evaluate whether:

- A firm's quality control system for its accounting and auditing practice appropriately addresses each element of quality control
- The quality control policies and procedures are adequately documented and communicated to professional personnel
- Personnel are complying with the policies and procedures
- The firm is complying with the SECPS membership requirements

16 Independent peer reviewers, that is, other audit firms, examine each firm's quality control system every three years. The peer reviewers examine both the design of the system and compliance with it, including a review of internal firm documents and selected audit reports and working papers. At the completion of the peer review, the peer reviewers issue a report on the effectiveness of the design of and compliance with the system. The report, similar to that rendered at the completion of an audit, may be unmodified, modified or adverse. The report also may refer to a separate letter of comments that enumerates deficiencies in the system of quality control that were noted during the peer review. (When the report is unmodified, it states that none of the deficiencies are of such significance as to result in a modified report.) The reviewed firm is required to submit a letter of response to the Peer Review Committee (PRC) describing the actions taken, or to be taken, by the firm to correct the deficiencies.

17 The peer review report and, if applicable, the letter of comments and letter of response (collectively, the peer review reports), together with the peer review working papers, are submitted to the POB staff or the SECPS staff for review. The POB staff performs an in-depth review of the peer review working papers and related peer review reports for those firms, including all of the largest firms, that meet its risk-based criteria. The POB staff provides oversight on all other peer reviews. The SECPS staff reviews the peer review working papers and related reports for those peer reviews that the POB staff does not review. Collectively, the SECPS and POB staffs then present the reports to the PRC (comprising representatives from 18 member firms) for acceptance. On acceptance, the peer review reports are placed in a public file at the AICPA.

18 When necessary, the PRC imposes corrective measures on member firms to make certain that quality control deficiencies are corrected. Those corrective measures and the number of times they were imposed during the SECPS's fiscal year ended June 30, 1999, and since the inception of the peer review process are as follows⁴:

⁴ Public Oversight Board, *Annual Report 1999*.

Action	<u>Year Ended June 30, 1999</u>	<u>Since Inception</u>
Accelerated peer review	1	54
Employment of an outside consultant to perform preissuance reviews of financial statements or other specified procedures	11	110
Oversight by the peer reviewers or a PRC member to monitor progress made by the firm in implementing corrective actions	11	220
Oversight of the firm's internal monitoring program	32	402
Changes made to the firm's quality control document or other guidance materials	1	44
Continuing professional education in specified areas	4	62*

* Since July 1, 1988; data for prior years are no longer available.

19 The POB oversees the entire peer review process, including reviewing the qualifications of peer reviewers. Further, under the provisions of an access agreement between the POB and the Office of the Chief Accountant (OCA) of the SEC, the peer review working papers and related reports (masked to protect the confidentiality of individual registrants) are made available for review and oversight by the OCA staff.

Quality Control Inquiry Committee

20 Shortly after the SECPS instituted the peer review process, its member firms and the SEC sought a means to address issues of alleged audit failures that occurred during the three-year period between a firm's peer reviews. The result was the Special Investigations Committee, later renamed QCIC, which consists of approximately 12 representatives of member firms, most of whom are retired.

21 Member firms are required to report to QCIC, within 30 days of being served, all matters of alleged audit failures involving SEC clients arising from litigation or regulatory investigations, including criminal indictments. The QCIC process begins almost immediately after a matter is reported; it is not deferred while litigation or regulatory proceedings are in process. The allegations are investigated by QCIC members and staff to determine whether there are deficiencies in the reporting firm's system of quality control, its compliance with the system, or the professional standards relevant to the matters in the case. QCIC does not make any determinations concerning the guilt, innocence or liability of the reporting firm.

22 The activities of QCIC take place in four distinct phases. Each case added to its agenda might require QCIC to employ the procedures in one or more phases. The phases and the related procedures are as follows:

Phase No. 1 – Analysis of allegations

23 Read the complaint against the firm, relevant financial statements and any other publicly available relevant materials. After evaluating the information, proceed to Phase No. 2 unless the case file can be closed because, after analysis, QCIC considers the complaint to be frivolous. A frivolous complaint is characterized by, among other things:

- Allegations that do not relate to a period in which the auditor was associated with the entity's financial statements
- Allegations that are so general in nature that they do not raise serious implications concerning the adequacy of the firm's system of quality control or its compliance with that system
- Allegations that ignore relevant and adequate disclosures made in the financial statements or information contained in the auditor's report
- Allegations that do not relate to matters that are encompassed by existing generally accepted accounting principles (GAAP) or generally accepted auditing standards (GAAS), or that clearly misstate their requirements

Phase No. 2 – General inquiries

24 Discuss the issues addressed by the allegations that have quality control implications with representatives of the firm. Based on those discussions, proceed to Phase No. 3 unless the case file can be closed because one or more of the following conditions exist:

- The relevant aspects of the firm's system of quality control are considered adequate based on QCIC's review of the firm's relevant guidance materials and established firm auditing or quality control policies and procedures
- The complaint stems from a business failure, not an audit failure
- Nothing more than minor changes in quality control were necessary, and the firm has taken appropriate corrective measures and has satisfied QCIC that those changes are effective

Phase No. 3 – In-depth inquiries

25 Discuss with firm personnel who are familiar with the subject engagement the quality control policies and procedures and compliance with them; review firm technical manuals, guidance materials and inspection reports; or read certain audit documentation having a bearing on the issues addressed by the allegations. Based on those procedures, proceed to Phase No. 4 unless the case file can be closed because the responses to QCIC's inquiries provide a reasonable

basis to conclude that the firm's quality control policies and procedures are adequate and were complied with.

Phase No. 4 – Special review

26 A special review is ordered whenever QCIC, based on its evaluation of responses to in-depth inquiries, is not satisfied that the firm's quality control system provides the firm with reasonable assurance of performing audit engagements in compliance with professional standards, whether for the firm as a whole, an office or a specific industry. The scope of a special review is directly related to the extent of the possible quality control deficiencies and any corrective actions that may be needed.

27 From July 1, 1981, through June 30, 2000, QCIC has opened 866 cases (see Table 2 to this appendix).

28 Before 1998, the AICPA Ethics Division would open a case file on the AICPA members on the engagement concurrent with QCIC opening a case file. The Ethics Division, as a matter of fairness to an AICPA member and at the member's request, would defer its investigation until the litigation or regulatory proceeding had been completed, which often was many years after the allegation had been made. Even when the QCIC investigation resulted in a determination that the allegation was frivolous, the Ethics Division would expend considerable time and resources (albeit many years later) to reach a similar conclusion.

29 In 1998, in an attempt to eliminate this waste of time and resources, the SECPS Executive Committee and the Professional Ethics Executive Committee (PEEC) entered into a Memorandum of Understanding (MOU) whereby QCIC would assign a rating to each case at the conclusion of its investigation, ranging from a "1" to a "4." The ratings and related recommendations are:

1. QCIC deems the case to be frivolous and recommends that no actions be taken by the PEEC with respect to the engagement personnel.
2. QCIC determines that no engagement personnel issues of significance are involved in the case and recommends that no actions be taken by the PEEC with respect to the engagement personnel.
3. QCIC believes that there may be engagement personnel issues of significance, and recommends that the PEEC determine whether or not to open an investigation of certain engagement personnel.
4. QCIC recommends that the PEEC open an investigation of certain engagement personnel.

30 Since the inception of the MOU, which was made retroactive to those cases closed by QCIC at its December 1997 meeting, a total of 125 cases have been rated, the results of which are:

<u>Rating</u>	<u>No. of cases</u>
1	12
2	64
3	38
4	11

31 As of August 2000, the PEEC has reviewed 36 of the cases rated as “3” and opened a case file on 28 of those matters. Noteworthy is the fact that the PEEC did not open a case file on 84 of the 125 cases, which allows it to devote additional time and resources to those cases that merit its scrutiny. In addition, QCIC has referred 25 current or former client personnel who are members of the AICPA to the PEEC.

32 The following table presents QCIC’s actions related to member firms, professional standards and individuals for the SECPS fiscal year ended June 30, 1999, and since the inception of QCIC⁵:

	<u>Year Ended June 30, 1999</u>	<u>Since Inception</u>
Actions related to firms		
Either a special review was made, the firm’s regularly scheduled peer review was expanded or other relevant work was inspected	2	72
The firm took appropriate corrective measures that were responsive to the implications of the specific case	6	133
Actions related to standards⁶		
Appropriate AICPA technical bodies were asked to consider the need for changes in, or guidance on, professional standards	3	49
PITF was asked to consider the issuance of a Practice Alert	2	23
Actions related to individuals		
The case was referred to the AICPA Professional Ethics Division with a recommendation for investigation into the work of specific individuals	14	46

⁵ Public Oversight Board, *Annual Report 1999*.

⁶ During its analysis of cases, QCIC is cognizant of the need to identify matters for which it believes the profession would benefit from additional or more specific standards or guidance. It refers these matters to the appropriate standard setters or the PITF for inclusion in a Practice Alert.

33 The POB oversees the QCIC process through its participation in all aspects of QCIC's analysis, investigation and closing of each matter. Further, the SEC staff reviews the Closed Case Summary prepared by the QCIC staff, together with the POB's oversight files for each matter.

SEC Regulations Committee

34 The SEC Regulations Committee acts as the primary liaison between the profession and the SEC on technical matters relating to SEC rules and regulations. It provides input to the SEC on accounting and auditing matters, as well as relevant guidance to AICPA members.

35 The SECPS Regulations Committee consists of representatives from SECPS member firms, academia and industry.

Professional Issues Task Force

36 The PITF was created by the SECPS Executive Committee to accumulate and consider practice issues that present potential audit concerns for practitioners from numerous sources, including QCIC, the PRC and the POB.

37 The PITF disseminates its information through non-authoritative Practice Alerts, which are published in the version of *The CPA Letter* that is distributed to AICPA members in public accounting firms. The Practice Alerts also are available on the AICPA's website. The PITF also refers matters that may require a reconsideration or reinterpretation of existing standards to appropriate standard-setting bodies.

38 The PITF consists of representatives from a number of SECPS committees, the ASB, PEEC and the legal departments of audit firms.

Firm Policies and Procedures

39 Audit firms establish, maintain and enforce firm-wide quality control policies and procedures. These measures are designed to provide each firm with reasonable assurance that it complies with professional standards, maintains its technical capabilities, applies the appropriate expertise on all audits and meets the SECPS membership requirements. Although invisible to the public, internal monitoring of audit quality is considered by many to be the most pervasive and productive of all types of regulation. The principal components of internal monitoring include periodic inspection procedures, determination of any corrective actions to be taken and improvements to be made in the quality control system, vigorous internal challenges regarding client acceptance and continuance decisions, independent preissuance reviews of audit engagements, and continuous updating of guidance and training materials and their dissemination to professional personnel. Enlightened self-interest has led firms to emphasize the importance of

quality control and to discipline professionals who depart significantly from firm policies and professional standards.

Standard-Setting Bodies

40 Professional standards form the basis for measuring performance. The standard-setting bodies in the accounting profession include:

Financial Accounting Standards Board

41 The federal securities laws give the SEC statutory authority for establishing accounting standards. In meeting this statutory responsibility, the SEC historically has looked to the standard-setting bodies designated by the profession to provide leadership in establishing accounting principles. Since 1973, that body has been the FASB.

42 The FASB, as part of the Financial Accounting Foundation (FAF), is a not-for-profit organization supported by contributions from accounting firms, corporations and other entities that are interested in accounting issues. The FASB consists of seven full-time members who are selected and approved by the FAF; the FASB establishes its agenda through discussions with parties interested in financial accounting.⁷ The FASB's deliberations are open to the public and its standards are subject to public exposure prior to issuance. The FASB maintains a dialogue with the SEC regarding its deliberations and activities.

43 In order to provide timely guidance to financial statement preparers, auditors and users on emerging issues that affect financial reporting, the FASB established the Emerging Issues Task Force (EITF). The EITF identifies emerging accounting issues and publishes its "consensus" in authoritative releases. The short time frame in which the EITF is expected to respond to the need for guidance does not permit preissuance public exposure of its pronouncements. The Chief Accountant of the SEC, who has the right to the floor, attends the EITF meetings as "the SEC Observer."

44 The Accounting Standards Executive Committee (AcSEC) of the AICPA promulgates GAAP on certain industry issues and other matters (e.g., software revenue recognition), under the FASB's oversight. Most AcSEC pronouncements are exposed for comment prior to issuance.

Auditing Standards Board

⁷ The FAF established the Financial Accounting Standards Advisory Council (FASAC) to advise the FASB on issues related to projects on the FASB's agenda, possible new agenda items, project priorities, procedural matters that may require the attention of the FASB, and other matters as requested by the FASB chairman.

45 After the highly publicized McKesson-Robbins audit failure in 1939, the AICPA established the predecessor committee to the ASB to promulgate GAAS. The ASB is funded by the AICPA through members' dues. Its pronouncements, which include quality control standards as well as GAAS, are subject to public exposure and comment. Like the FASB, the ASB maintains a dialogue with the SEC regarding its activities and deliberations. The ASB's pronouncements are applicable to audits of all entities, not just to audits of public companies; however, certain Statements on Auditing Standards (SASs) are applicable primarily to public company engagements (e.g., SAS No. 71, *Interim Financial Information*).

46 The ASB consists of 15 members, with representatives from audit firms, academia and government (either state or federal government entities). The AICPA Board of Directors approves the membership of the ASB.

AICPA Ethics Division

47 After the creation of the SEC, the AICPA adopted certain auditor independence rules that were necessitated by the SEC's requirement for audits by independent accountants. Subsequently, the AICPA formed its Ethics Division, which, through the PEEC, is responsible for changes to and determining compliance with the profession's Code of Professional Conduct. Unlike the SEC, the Ethics Division does not have subpoena power and its disciplinary authority extends only to individual AICPA members. As previously noted, its disciplinary process is deferred while litigation or regulatory proceedings are in process.

Independence Standards Board

48 The ISB was established in 1997 by the SEC and the AICPA for the purpose of assuming responsibility from the SEC for establishing standards for auditor independence with respect to audits of public companies. The ISB is funded by the SECPS, but it is an autonomous body with responsibility for hiring and supervising its staff, establishing its budget and, with input from the SEC, determining its agenda.

49 The ISB consists of eight members, of whom four are public members and four are from the accounting profession. Three of the accounting profession members, who are nominated by the SECPS Executive Committee, are representatives of SECPS member firms, and the fourth is the President of the AICPA or his or her designee. The public members are responsible for nominating their successors. The SECPS-nominated ISB members must be approved by the AICPA Board of Directors.

50 In accordance with SEC Financial Reporting Release No. 50 issued in December 1997, standards issued by the ISB will be deemed by the SEC to have "substantial authority" regarding matters of auditor independence with respect to audits of public companies; however, ISB standards that are less restrictive than existing SEC or AICPA rules will not be effective until the SEC or the AICPA amends or revokes its rules. (The

PEEC retains responsibility for all other matters contained in the Code of Professional Conduct, including the rules relating to independence for audits of all other entities.)⁸

⁸ In May 2000, the PEEC stated that it would view any pronouncement issued by the ISB as authoritative for *any* engagement requiring independence unless and until the PEEC announces that it will not view that pronouncement as authoritative. Accordingly, if an AICPA independence standard is more restrictive, in whole or in part, than an ISB pronouncement, the PEEC will not consider a member's independence to be impaired as a result of his or her non-compliance with the more restrictive AICPA standard until members are given notice of the PEEC's rejection of the ISB's less restrictive pronouncement.

CURRENT GOVERNANCE STRUCTURE

TABLE 1

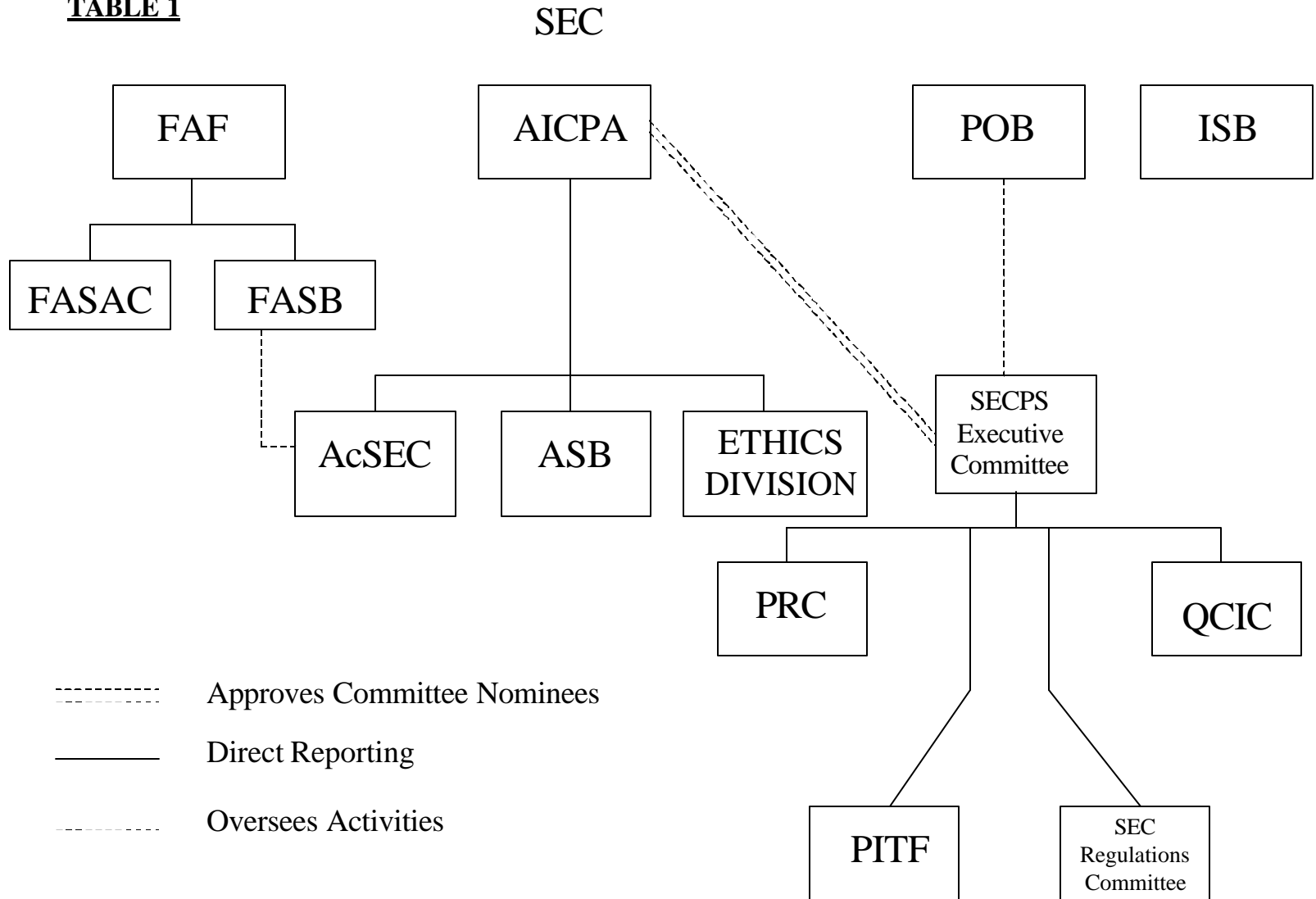


TABLE 2

**Quality Control Inquiry Committee
Number of Cases Reported to QCIC by Year**

Year Ended June 30,	Number of Cases
1982	20
1983	34
1984	27
1985	47
1986	44
1987	44
1988	42
1989	53
1990	56
1991	44
1992	55
1993	59
1994	61
1995	51
1996	33
1997	37
1998	53
1999	48
2000	58
Total	866