

**OPENING STATEMENT OF
RANKING DEMOCRATIC MEMBER PAUL E. KANJORSKI
SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE,
AND GOVERNMENT SPONSORED ENTERPRISES
SECOND HEARING ON CORPORATE ACCOUNTING PRACTICES:
IS THERE A CREDIBILITY GAAP?
TUESDAY, MAY 14, 2002**

Mr. Chairman, we meet again today to learn more about problems with corporate accounting practices. The many recent news reports of corporate accounting problems have raised numerous questions about whether our Nation's accounting principles and practices provide sufficient guidance to management, corporate directors, and auditors.

As you know, Mr. Chairman, I have held serious reservations about the reliability of certain corporate accounting practices for some time. If not fixed in the short term, these problems could have potentially serious and negative consequences for our country's flourishing capital markets in the long term. After all, if investors cannot trust the reliability of the numbers produced by corporate accountants in audited statements, then they might as well spend their hard-earned money on lottery tickets.

Today's hearing furthers the investigations that we began earlier this month. Our capital markets are the most successful in the world for one simple reason -- investor confidence. The transparency fostered by the application of Generally Accepted Accounting Principles has played an important role in this success. In fact, former Treasury Secretary Lawrence Summers has suggested that the development of GAAP was one of the most important innovations in the history of our capital markets, because that standardization enabled investors to compare and contrast the performance of companies. Unfortunately, the failure to implement GAAP consistently has now led to an almost daily discovery of accounting irregularities at American corporations. This evolving situation has also sparked a crisis of confidence that continues to ripple through our capital markets.

We have, however, known about these problems for some time. For example, research published in 2001 by Financial Executives International identified some startling facts. The study found 464 cases of earnings restatements in corporate America over a three-year period, more than the previous seven years combined. It also determined that 156 earnings restatements in 2000 wiped out more than \$31 billion in market capitalization. I suspect that when we tabulate these figures for 2001, these two already sizable statistics will grow considerably.

What factors contributed to this troubling state of affairs? In recent decades, the rules governing corporate accounting have become increasingly complex. Since the early 1990s, for example, the Financial Accounting Standards Board has developed several fair-value measurement, recognition, and disclosure standards. These standards often permit multiple interpretations. Accounting has also evolved from determining the cost of producing and the revenue from selling a good like a screwdriver, to ascertaining the cost and revenue from selling an intangible service like a 25-year energy derivative. These and other developments have helped to make corporate financial statements increasingly impenetrable and confusing.

From my perspective, an effective accounting system must ensure the comparability of financial data from one company to another. Comparability in the data used by investors will

allow them to evaluate apples against apples, and oranges against oranges. Improvements in accounting transparency will also facilitate the efficient flow of capital.

Today's hearing will help us to examine the roles of the Securities and Exchange Commission and the Financial Accounting Standards Board in developing Generally Accepted Accounting Principles. Throughout its history, the Securities and Exchange Commission has relied on the private sector to establish accounting standards. We will explore today whether that policy should continue.

We will also explore today whether we should move from a "rules-based" accounting system to a "principles-based" accounting regime. International accounting standards presently rely more on principles and general guidelines than the American system. As the participants in our global economy become increasingly interdependent, it may be time for us to modify our own accounting regime. I approach this debate with an open mind.

In closing, Mr. Chairman, I believe our Committee should comprehensively explore the issues related to corporate accounting practices, and I am looking forward to hearing from our distinguished witnesses.
