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The following comments are submitted regarding  
PCAOB Rulemaking Docket Matter No. 003

## Ethics Code

### Introduction

The goal set forth in the introductory remarks – that “The Board must ensure that its own business integrity, values and principles are above reproach” is worthy and necessary in the circumstances. It should be a model for adoption by registered firms. As noted below, the proposed ethics code is not sufficient in many respects to assure this goal’s achievement.

### General comments

In spite of the introductory statement lauding the importance of values, the Code does not set forth any values that should be followed by those subject to it. Several of the values set forth in the AICPA Code of Professional Conduct represent a minimum that should be set forth in the Code. These include Integrity, Priority of the Public Interest, Objectivity and Independence, and Due Care. Other values that should be considered include Competence and Confidentiality.

The Code is also deficient in failing to sufficiently describe the measures needed for its successful administration. The Defense Industry Initiative rules and US Sentencing Guidelines’ description of mitigating circumstances should be set forth as a minimum. The administrative steps should describe the functions of training in the Code, monitoring its use, a confidential reporting or help-line, and other steps to make sure the Code is understood and used by all and not just a closeted unimportant document. The public will not have confidence in the activities of a Board that realizes it should have exemplary governance including ‘best practice’ ethics, but which in fact does not measure up.

### Specific comments

EC3. The General Principles should discuss in more depth but still general terms how the values underlying the Code’s provisions are to be applied. The language in the current draft is too unspecific to be very helpful in guiding the behavior of those subject to the Code. Best Practice ethics systems require a values approach, as hinted in the Board’s introduction, rather than legalistic provisions that are unlikely to motivate ethical behavior.

The analysis of EC3(b) discusses “the appearance of certain situations” that may not be “specifically prohibited by the Code.” This language is unlikely to be helpful in guiding behavior and illustrates the need for a values-based approach to motivating ethical behavior rather than a legalistic approach that presumes any behavior not specifically prohibited must be acceptable.

EC4 is titled Financial and Employment Interests, yet covers only financial but not employment matters. It should specifically state that no Board member or professional staff should enter into any outside employment except as provided in EC6. Particularly avoided should be any relationships with public accounting firms or issuers. The appearance of potential conflicts of interest will not permit the Board or staff to play a variety of different roles while still appearing to be objective in dealing with public accounting firms or issuers.

EC5 contains a prohibition on disclosing confidential information within the context of investments. As noted above, Confidentiality should be a keystone value of the Board and its staff and for emphasis should be discussed in a general context, not just as it relates to investments.

EC6(b) should provide for prompt public disclosure of any waivers of the Code granted under this section to be consistent with the Sarbanes Oxley Section 406 requirement for issuers. As noted below, it is not obvious what benefit there is to the public interest or the Board's mission of helping to restore and then maintain confidence in the integrity of the securities markets for the Board or staff to be involved with outside employment. If this section contemplates allowing an activity like writing a book that would guide firms and issuers, such an example should be set forth as guidance.

EC6(c)(3) uses the terms independence and objectivity as terms of art, yet these terms are not set forth in the Code as underlying values nor described as general principles (see above). At least they should be defined for use in this context. This comment also applies to EC8(a).

The analysis of EC6(c)(3) is incorrect in stating that the three concepts describing precluded outside activities are "self-explanatory." Rather, they do require explanation as they include terms used ambiguously in varying contexts. Further, examples of activities that are acceptable, if any, should be set forth for the continuing guidance of the Board and staff.

EC6(c)(3) should also make it clear that any relationships involving public accounting firms or issuers should be avoided. As noted above, it is not obvious what benefit there is to the public interest for the Board or staff to be involved with any activities other than their principal employment that is directed toward the Board's mission of helping to restore and then maintain confidence in the integrity of the securities markets.

EC9 would be strengthened by inclusion of Confidentiality as an underlying value and General Principle (see above).

EC11 does not describe current best practice for Ethics Officers. An Ethics Officer should report directly to the Board and have responsibilities for administering the ethics system. At its website: [www.eoa.org/Whatis.asp](http://www.eoa.org/Whatis.asp), The Ethics Officer Association describes responsibilities of ethics officers in terms of a senior executive that administers the ethics system in an organization. Specific responsibilities can include:

- Global accountability for developing and directing an organization's ethics, compliance, and business conduct function for the total organization.
- Accountability for the organization-wide confidential reporting program

- Setting the strategy for and administering the organization's annual or periodic ethics and compliance training, and regular communications around ethics, compliance and business conduct issues
- Conducting investigations into alleged violations of company ethics, compliance or business conduct practices and making recommendations for resolution of misconduct
- Providing leadership, oversight, and expert advice to ensure appropriate development, interpretation, and implementation of ethics and compliance strategies, policies and programs

EC13. The Code should state what circumstances, if any, that would benefit the Board's mission by granting any waivers of the Code. Waivers, if any, should not be left to the total discretion of an individual and allowed for a wide spectrum of reasons. It is not obvious what benefit there is to the public interest for the Board or staff request a waiver of the Code. The Code should enhance the public image of the Board and staff and motivate them to direct their full energies toward the Board's principal mission of helping to restore confidence in the securities markets.

EC13. The Board should also not delegate responsibility for granting waivers of the applicability of the Code. Waivers for the Board or staff should be few, if any, because the practice of granting a waiver sends the signal that an ethics code need apply only when convenient. This was the message the Enron Board ethics waiver sent to its staff with devastating results. Also, any waivers granted should be promptly made public to conform the Board's and public accounting firm practices with those required by Sarbanes-Oxley for issuers.

EC 13 should either be deleted or its language revised to state that waivers will only be granted to further the interests or reputation of the Board, NOT that any cause not demonstrably harmful should be acceptable.

EC14. As mentioned previously, mere annual rote certification of compliance is insufficient as the only administrative function designed to ensure compliance with the spirit of the Code. Regular training, emphasis as an element of staff performance evaluation, and a system of confidential communication or help-line should be added to this section.

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