

financial statements of public companies; and

- Whether the person has any other relevant qualifications or experience that would assist him or her in understanding and evaluating the registrant's financial statements and other financial information and to make knowledgeable and thorough inquiries whether:

- The financial statements fairly present the financial condition, results of operations and cash flows of the company in accordance with generally accepted accounting principles; and

- The financial statements and other financial information, taken together, fairly present the financial condition, results of operations and cash flows of the company.

b. *Comments on Proposed Definition.* The proposed definition of the term "financial expert" proved to be the most controversial aspect of the proposals—more commenters remarked on it than on any other topic addressed by the proposed rules. Most of the commenters thought that the proposed definition was too restrictive. Several expressed concern that many companies, especially small ones, would have a difficult time attracting an audit committee member who would qualify as an expert under the proposed definition. Some of the corporate commenters were of the view that they already have exemplary audit committees, despite the fact that none of their current members would meet our proposed definition of an expert. A few complained that companies may have to sacrifice the diversity of their boards and nominate directors who satisfy the audit committee financial expert definition even if the company does not believe that these directors are best-suited for the position.

Furthermore, several commenters debated the merits of defining an audit committee financial expert as a person with strong accounting credentials, given that an audit committee member's role is one of oversight, rather than direct involvement in the company's accounting functions, and suggested that the emphasis on technical accounting expertise in the definition was misplaced. A few commenters further argued that it is unnecessary to have a financial expert serving on the audit committee because audit committee members should have the discretion to retain experts with specific financial expertise as they deem necessary or appropriate.

Other commenters asserted that the proposed definition was more restrictive than necessary to satisfy Congressional intent—they noted that Section 407 of

the Sarbanes-Oxley Act requires us, in defining the term "financial expert," only to "consider" whether a person has, through education and experience as a public accountant, auditor, principal financial officer, comptroller, principal accounting officer, or similar position, the four attributes specified in the Act.²⁴ These commenters argued that in light of the Congressional directive only to consider the four attributes, our proposed definition did not need to incorporate all of them, or even any of them. Some commenters believed that a single member of the audit committee should not have to possess all of the required financial expert attributes so long as the members of the audit committee collectively possess these attributes. Others suggested various permutations such as requiring the financial expert to have the first and fifth attributes in our proposed definition, but only two of the other three attributes.

Many commenters criticized specific provisions of the proposed financial expert definition as being too narrow. In particular, many commenters asserted that our proposed requirement that an expert have direct experience preparing or auditing financial statements was greatly, and needlessly, restrictive. Other commenters were concerned that the requirement that a person have had experience with financial statements presenting issues generally comparable to those raised by the company's financial statements might have anti-competitive effects if we interpreted this requirement to mean that a financial expert would need previous experience with financial statements of other companies in the same industry.

Several commenters sought clarification regarding the relevant body of generally accepted accounting principles, in particular for financial experts of foreign private issuers. Other commenters expressed concern over the possible lack of potential financial experts that would be knowledgeable about accounting for estimates and reserves in specific industries, such as the insurance and oil industries.

Numerous additional commenters were concerned that the proposed

definition was too restrictive regarding the means by which a person could acquire the required expertise to qualify as a financial expert. They suggested that a requirement that an expert have experience as a public accountant, auditor, principal financial officer, controller, principal accounting officer or in a similar position, would severely limit the number of persons qualified to be financial experts. Some believed that there are a substantial number of highly qualified persons who have sufficient knowledge and experience to effectively and competently perform the activities required of a financial expert, but do not have experience in one of the listed positions. They questioned the relevance of the means by which a person acquires the necessary expertise, so long as the person in fact has such expertise.

c. *Final Definition of "Audit Committee Financial Expert"*. The final rules define an audit committee financial expert as a person who has the following attributes:

- An understanding of generally accepted accounting principles and financial statements;
- The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;
- Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities;
- An understanding of internal controls and procedures for financial reporting; and
- An understanding of audit committee functions.²⁵

Under the final rules, a person must have acquired such attributes through any one or more of the following:

- (1) Education and experience as a principal financial officer, principal accounting officer, controller, public accountant or auditor or experience in one or more positions that involve the performance of similar functions;
- (2) Experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor or person performing similar functions;

²⁴ The attributes listed in Section 407 of the Sarbanes-Oxley Act include:

- (1) An understanding of generally accepted accounting principles and financial statements;
- (2) Experience in: (a) The preparation or auditing of financial statements of generally comparable issuers; and (b) the application of such principles in connection with the accounting for estimates, accruals, and reserves;
- (3) Experience with internal accounting controls; and
- (4) An understanding of audit committee functions.

²⁵ See new Item 401(h)(2) of Regulation S-K, Item 401(e)(2) of Regulation S-B, Item 16A(b) of Form 20-F and paragraph (8)(b) of General Instruction B to Form 40-F.