

Private Sector: Accounting and Auditing Regulatory Structure

August 26, 2025

Congressional Research Service

<https://crsreports.congress.gov>

R48647



R48647

August 26, 2025

Raj Gnanarajah
Analyst in Financial
Economics

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In the United States, accounting and auditing standards are promulgated and regulated by various federal, state, and self-regulatory agencies. Accounting and auditing standards are also influenced by practitioners from businesses, nonprofits, and government entities (federal, state, and local). Many of the foundational accounting and auditing concepts are similar across all three sectors. Congress has allowed financial accounting and auditing practitioners in the private sector to remain largely self-regulated while retaining oversight responsibility. At times, Congress has sought to achieve specific accounting- and auditing-based policy objectives by enacting legislation such as the Sarbanes-Oxley Act of 2002 (P.L. 107-204) and Holding Foreign Companies Accountable Act (HFCAA, P.L. 116-222).

The accounting and auditing standards created for publicly traded companies (private sector) are subject to oversight by the Securities and Exchange Commission (SEC). Congress has oversight over the SEC and annually appropriates its funding. Throughout its history, the SEC has relied on self-regulatory organizations (SROs) or similar entities to establish financial reporting standards for the private sector known as Generally Accepted Accounting Principles (GAAP). Currently, the SEC recognizes the Financial Accounting Standards Board (FASB) as the designated authority for establishing GAAP. Sarbanes-Oxley created the Public Company Accounting Oversight Board (PCAOB) to oversee the auditing profession for the private sector. The SEC has oversight responsibility over FASB and PCAOB.

Some of the ongoing issues that could be of interest to Congress is the accounting treatment of crypto assets. In March 2022, the SEC issued Staff Accounting Bulletin (SAB) 121 to provide guidance for how custodians of crypto assets should record and measure the value of assets they held on behalf of others. One aspect of SAB 121 that surfaced a range of perspectives was its requirement of a crypto asset custodian to record a liability and corresponding asset on its balance sheet. Subsequently, in January 2025, the SEC issued SAB 122 rescinding SAB 121. Despite rescinding SAB 121, SAB 122 includes reminders that existing GAAP financial reporting requirements related to disclosure, risk of loss, and change in accounting methodology are still applicable.

Seeking to prevent requirements similar to SAB 121 from being imposed on crypto asset custodians, the House passed a Digital Asset Market Clarity Act of 2025 (H.R. 3633) in July 2025. While it is designed to provide a system of regulation for the offer and sale of digital commodities, it contains provisions that would limit the ability of the banking and financial regulators to impose requirements similar to SAB 121, such as recording a liability and corresponding asset on the balance sheet.

Other issues of potential congressional interest surround the PCAOB. Congress passed HFCAA to address audit limitations faced by the PCAOB. HFCAA requires foreign companies listed in U.S. stock exchanges to be subject to the same accounting and audit oversight as listed domestic companies. The law requires the SEC to identify each foreign firm not in compliance and suspend trading of those companies from U.S. exchanges after three years of noncompliance.

Separately, an initial House-passed version of H.R. 1, then-named the One Big Beautiful Bill Act, included provisions that would have transferred the functions of the PCAOB to the SEC. A similar provision was proposed by Senator Tim Scott in the Senate, but it was reportedly determined to be in violation of the Byrd rule. The provisions were not included in the enacted version of the FY2025 reconciliation act (P.L. 119-21).

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Introduction

Accounting is commonly considered the language of business.¹ A common set of principles and rules help establish accounting standards. Accountants who audit financial statements (auditors²) also adhere to a common set of audit principles and rules to examine financial statements.

Congress has allowed financial accounting and auditing practitioners in the private sector to remain largely self-regulated while retaining oversight responsibility. At times, Congress has sought to achieve specific accounting- and auditing-based policy objectives related to the private sector by enacting legislation such as the Sarbanes-Oxley Act of 2002 (SOX)³ and Holding Foreign Companies Accountable Act (HFCAA).⁴

This report examines the U.S. accounting and auditing regulatory structure for the private sector. It first provides background on why different accounting standards exist between the private and public sectors. It then discusses how accounting and auditing standards are created and regulated in the private sector. Some of the policy issues discussed in this report include accounting for crypto assets, the Public Company Accounting Oversight Board (PCAOB), challenges in examining foreign audit firms' work papers, and the effects of transferring PCAOB functions to the SEC as initially considered under earlier versions of H.R. 1 (originally called the One Big Beautiful Bill, which would go on to be enacted as P.L. 119-21 without the PCAOB related provisions included). **Appendix A** provides a glossary that explains the various financial statements listed in **Table 1**. **Appendix B** provides the Principles of Professional Conduct for Certified Public Accountants (CPAs) from the American Institute of Certified Public Accountants (AICPA).

Background

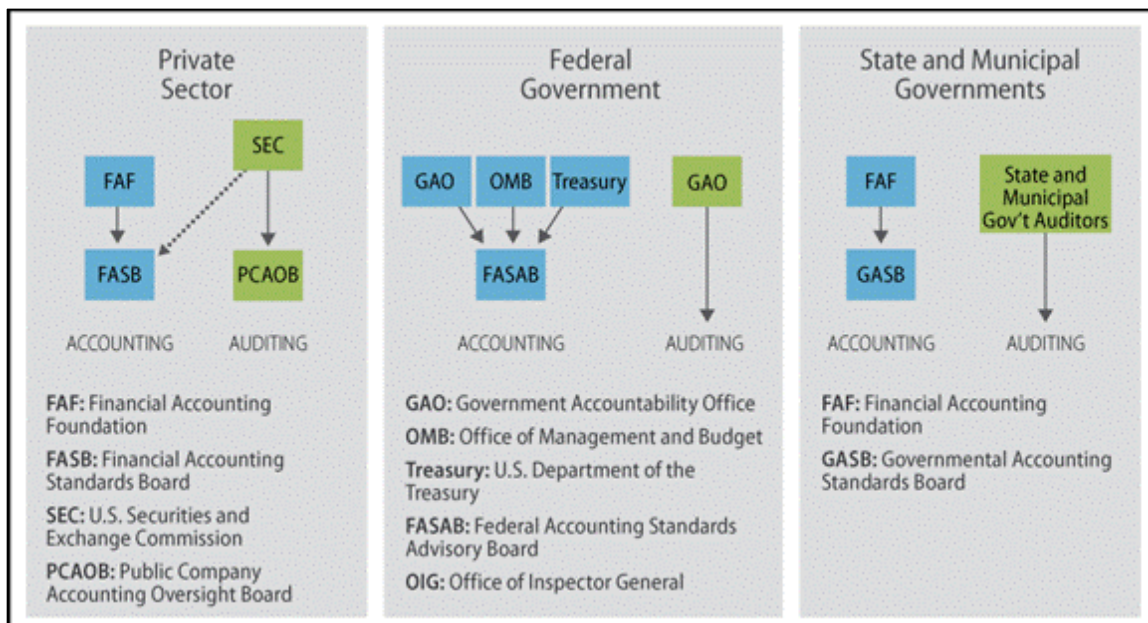
The informational needs of stakeholders differ between the private and public sectors. As a consequence, different accounting and auditing standards have evolved in these sectors to address stakeholders' specific needs. In the private sector, financial statements communicate to stakeholders—such as investors, creditors, company employees, regulators, and others—how the company used its resources to generate profit and expand its business or how the company incurred loss and the likelihood the business will survive over the long run. Public-sector entities such as the federal, state, and local governments issue reports to communicate how tax revenues were used to benefit citizens. Their intended audience is usually taxpayers, Congress, or the state and local legislatures. State and local governments have standards distinct from those of the federal government. Thus, accounting and auditing standards can be classified into three areas: (1) private industry standards, (2) federal government standards, and (3) state and local government standards. **Figure 1** provides an overview of the accounting and auditing standard-setters for the different segments previously mentioned.

¹ CNBC, "CNBC Excerpts: Billionaire Investor Warren Buffett on CNBC's 'Squawk Box' Today," March 2, 2015, <https://www.cnbc.com/2015/03/02/cnbc-excerpts-billionaire-investor-warren-buffett-on-cnbc-squawk-box-today.html>.

² Financial statement auditors are accountants who have specialized training as auditors. Program or statutory auditors can be accountants or others who have received specialized training.

³ P.L. 107-204.

⁴ P.L. 116-222.

Figure 1. Accounting and Auditing Standard-Setters

Source: CRS. Financial Accounting Foundation (FAF), "About the FAF," <https://www.accountingfoundation.org/about-us/about-the-faf>.

Notes: In the first panel, the striated line indicates the SEC's oversight role over accounting standards promulgated by the FASB. The FASB's parent organization, FAF, is a nonstock Delaware corporation. Neither FASB nor FAF is a government agency, even though the SEC does have oversight of the budget for FASB and the accounting standards as promulgated by FASB.

Private Sector

In the private sector, financial statements provide economy-wide benefits to firms and investors through the dissemination of accurate information. One way these benefits are realized is through the efficient allocation of capital between investors and firms.⁵ Investors rely on financial statements to make informed decisions on how best to invest their savings. Financial statements are a primary means by which firms communicate with capital markets, investors, creditors, regulators, the public, and others. **Figure 2** illustrates the range of private sector stakeholders.

⁵ Nonprofit entities' financial reporting focuses on how resources are used to benefit the intended purpose of the nonprofit. The standard of measure is the proportion of the donations used for administrative expenses versus operating expenses.

Figure 2. Stakeholders in the Private Sector

Source: Adapted from PWC, “Understanding a Financial Statement Audit,” May 2017, p. 3, <https://www.pwc.com/im/en/services/Assurance/pwc-understanding-financial-statement-audit.pdf>.

The private sector includes publicly traded and privately held companies as well as nonprofit organizations. Privately held companies (non-public firms) are not required by regulators to use the same accounting standards as publicly traded firms are, but non-public firms often use the same standards to have equal access to credit and for either eventually going public or as preparation for a buyout or merger, among other reasons. This report focuses on publicly traded companies.⁶ The accounting and auditing standards created for publicly traded firms are subject to oversight by the Securities and Exchange Commission (SEC).⁷ Congress created the SEC in 1934 to protect investors and to maintain fair, orderly, and efficient markets. However, Congress has oversight over the SEC and annually appropriates its funding.⁸ Currently, the SEC recognizes the Financial Accounting Standards Board (FASB) as the designated authority for establishing accounting standards. SOX created PCAOB to oversee the auditing profession for the private sector. The SEC has oversight responsibility over FASB and PCAOB.

Accountants and auditors, in addition to adhering to accounting and auditing standards, are also subject to the ethical requirements of their affiliated membership organizations, such as CPAs’ Principles of Professional Conduct (see **Appendix B**).

⁶ A more detailed discussion of non-public firms is beyond the scope of this report. For more information, see Financial Accounting Foundation, “GAAP and Private Companies,” <https://accountingfoundation.org/accounting-and-standards/about-gaap/gaap-and-private-companies>.

⁷ For more information about the SEC, CRS Report R48521, *Capital Markets and Securities Regulation: Overview and Policy Issues*, by Eva Su.

⁸ For information about the SEC appropriations and funding, see CRS Report R48188, *Financial Services and General Government (FSGG) FY2025 Appropriations: Overview*, by Baird Webel.

Accounting

Accounting is a process by which an entity identifies, measures, and communicates financial information about its economic activities to stakeholders by adhering to a common set of practices, known as Generally Accepted Accounting Principles (GAAP).⁹ The primary way for an entity to communicate its financial performance to its stakeholders is through financial statements. In simple terms, accounting standards are agreements among practitioners (i.e., accountants, auditors, and regulators) on how each line item on the financial statement should be valued and reported.¹⁰

One of the powers Congress gave the SEC is the statutory authority to establish accounting standards for the private sector in the United States. Since the creation of the SEC, domestic companies have used GAAP to issue financial statements,¹¹ and the SEC has relied on the private sector to establish and develop GAAP.¹² Currently, the SEC recognizes FASB as the designated organization for establishing GAAP for the private sector.¹³

FASB Funding

Since enactment of SOX, FASB has been funded by fees collected from issuers of publicly traded securities. The fees are subject to SEC review.¹⁴ FASB incurred \$46.1 million in operating program and support expenses in 2024. The expenses were paid in part with \$42.9 million from accounting support fees.¹⁵ The remainder was paid through other revenue sources, such as the sale of publications and subsidies from FAF's excess reserve funds. FASB is a subsidiary of FAF. FAF, FASB, and Government Accounting Standards Board are mainly funded through accounting support fees, according to FAF.¹⁶

⁹ Each set of accounting standards that is created for a specific purpose can be considered GAAP. As an example, the private sector GAAP is different from accounting standards created for the federal government. Similarly, state and local government GAAP differ from private or federal government GAAP. Although creditors and other stakeholders may require private companies to follow GAAP, they are not required to follow GAAP unless they are registered with the SEC.

¹⁰ The field of accounting can be subdivided into different categories, such as financial accounting, tax accounting, managerial or cost accounting, and budget accounting (commonly used by the government sector). The annual report issued by private and public sector entities communicate to their respective stakeholders how the resources of the entity were used to meet the mission of the organization. The annual report might not only contain financial statements but might disclose and share information from other fields of accounting, such as tax accounting and cost accounting.

¹¹ The SEC issued a rule in 2007 that allows foreign issuers of financial statements to file with the SEC using International Financial Reporting Standards without having to reconcile to GAAP. SEC, "Foreign Issuer Information," June 22, 2016, <https://www.sec.gov/divisions/corpfin/cfforeignissuers.shtml>; and SEC, *Form 20-F*, July 2024, pp. 3, 5-6, <https://www.sec.gov/files/form20-f.pdf>.

¹² SEC, "Policy Statement: Reaffirming the Status of the FASB as a Designated Private-Sector Standard Setter," August 25, 2003, <https://www.sec.gov/rules-regulations/policy-statements/33-8221>.

¹³ The FASB's parent organization, the Financial Accounting Foundation (FAF), is a nonstock Delaware corporation. Neither FASB nor FAF is a government agency, even though the SEC does have oversight of the budget for FASB and the accounting standards as promulgated by FASB. FAF, "About FAF," <https://www.accountingfoundation.org/aboutfaf>.

Certain characteristics define a Delaware nonstock corporation, such as that it does not issue stock to raise capital and that, instead of shareholders, it will typically have members and with some exceptions does not have a profit motive. Government of the State of Delaware, *Title 8 Corporations, Chapter 1. General Corporation Law*, Delaware Code Online, <https://delcode.delaware.gov/title8/c001/sc01/>.

¹⁴ 15 U.S.C. §7219.

¹⁵ FASB, *Financial Statements for the Years Ended December 31, 2024 and 2023*, March 12, 2025, p. 5, <https://www.accountingfoundation.org/page/ShowPdf?path=FASB%20Audited%20Financial%20Statements%202024%20and%202023.pdf>.

¹⁶ FAF, "FASB, GASB, FAF: How We're Funded," <https://www.accountingfoundation.org/about-us/faf-fasb-gasb-how-we-are-funded>.

Financial statements for a publicly traded company or a privately held companies commonly include an income statement, a balance sheet, a statement of shareholder equity, and a statement of cash flows. **Table 1** compares the different financial statements presented in annual reports of various entities in different sectors. (For an explanation of different statements, see **Table A-1**.) As previously discussed, as a consequence of the differences between the private sector and the public sector, the financial statements normally used in one sector might not exist in the other. Further, financial statements within the same sector (e.g., the private sector) will communicate qualitatively different sets of information based on their underlying business activities. As an example, the financial statements for Boeing—mainly a manufacturer of commercial jetliners and defense, space, and security systems—will be qualitatively different from those of T-Mobile, a provider of cell phone service and retailer of cell phones.

Table 1. Comparison of Financial Statements in Various Sectors

Private Sector ^a	Federal Government ^b	State and Local Governments ^c
Income Statement	Statement of Operations and Changes in Net Position	Statement of Activities
Balance Sheet	Balance Sheet	Statement of Net Position (Assets)
Statement of Shareholders' Equity	Statement of Operations and Changes in Net Position	Statement of Net Position (Assets)
Statement of Cash Flows	Statement of Changes in Cash Balance from Unified Budget and Other Activities	Statement of Activities
Not Applicable	Statement of Net Cost	Required Supplementary Information
Not Applicable	Reconciliations of Net Operating Cost and Unified Budget Surplus (Deficit)	Required Supplementary Information
Not Applicable	Statement of Social Insurance	Required Supplementary Information
Notes to the Financial Statements	Notes to the Financial Statements	Notes to the Financial Statements
Management's Discussion and Analysis of Financial Condition and Results of Operation ^d	Management's Discussion and Analysis	Management's Discussion and Analysis
Management's Discussion and Analysis of Financial Condition and Results of Operation	Understanding the Financial Report of the United States Government ^e	Letter of Transmittal
Management's Discussion and Analysis of Financial Condition and Results of Operation	Required Supplementary Information	Required Supplementary Information
Management's Discussion and Analysis of Financial Condition and Results of Operation	Budget of the U.S. Government ^f	Statistical Section

Source: CRS.

Notes:

- a. Many of the financial statements in the government sector do not exist in the private sector or are not relevant.
- b. The financial statements listed below are from the *Financial Report of the United States Government: Fiscal Year 2024*. The financial statements listed in **Table 1** provide a comparison to the private sector. Individual agency financial reports may differ based on their function and purpose from what is listed for the federal government. See Department of the Treasury, *Financial Report of the United States Government: Fiscal Year*

2024, January 16, 2025, [https://www.fiscal.treasury.gov/files/reports-statements/financial-report/2024/01-16-2025-FR-\(Final\).pdf](https://www.fiscal.treasury.gov/files/reports-statements/financial-report/2024/01-16-2025-FR-(Final).pdf).

- c. The financial statements listed below are from the Annual Comprehensive Financial Report of the State of Ohio. Other states' and territories' financial statements might differ due to their respective laws and requirements. Only government-wide financial statements are included, and specific fund financial statements—such as proprietary funds, fiduciary funds, and fiduciary component units—are not listed. See State of Ohio, *State of Ohio: Annual Comprehensive Financial Report: Fiscal Year Ended June 30, 2024*, December 18, 2024, https://archives.obm.ohio.gov/Files/State_Accounting/Financial_Reporting/Comprehensive_Annual_Financial_Report/2024/ACFR_2024.pdf.
- d. Some elements of the various statements and schedules in the government sector might be similar in the management's discussion and analysis of financial condition and results of operation in the private sector, but most elements are not relevant or are not presented.
- e. U.S. Government Accountability Office, *Understanding the Financial Report of the United States Government*, GAO-18-239SP, February 15, 2018, <https://www.gao.gov/products/gao-18-239sp>.
- f. For the purpose of this table, the federal budget includes all supporting schedules. See Office of Management and Budget, "President's Budget," <https://www.whitehouse.gov/omb/information-resources/budget/>.

Annual Report to the SEC: Form 10-K

Federal securities laws require public companies, both domestic and foreign, to share critical information about their performance on an ongoing basis. Domestic companies are required to submit annual reports on Form 10-K, quarterly reports on Form 10-Q, and current events on Form 8-K. Form 10-K provides a comprehensive overview of the company's performance, including audited financial statements, and is required to be filed 60-90 days after the fiscal year end based on the size of the company. Form 10-Q is required to be filed 40-45 days after quarter end.¹⁷ Form 8-K is required to be filed within four business days of material corporate events to inform shareholders of such events. Companies submit their forms (reports) electronically to the SEC's Electronic Data Gathering, Analysis, and Retrieval system.

Based on the expectation that the United States will eventually either adopt or converge with International Financial Reporting Standards (IFRS),¹⁸ the SEC in 2007 changed the requirement for foreign private issuers (FPIs).¹⁹ Until 2007, foreign and domestic firms had similar filing requirements with the SEC. In 2007, to prevent foreign firms from potentially delisting from U.S. exchanges, the SEC authorized foreign firms to use their own domestic GAAP, which is often IFRS. In June 2025 the SEC began soliciting public comment on the definition of FPI, as it has not changed since early 2000s, although the population of FPIs has changed. In the press release seeking comments, SEC Chairman Paul Atkins stated:

Attracting foreign companies to U.S. markets and providing U.S. investors with the opportunity to trade in those companies under U.S. laws and regulations remains an objective. That objective must be balanced with other considerations, including providing investors with material information about these foreign companies, and ensuring that

¹⁷ SEC, "Glossary: F," <https://www.investor.gov/introduction-investing/investing-basics/glossary/f>.

¹⁸ A comparable accounting standard similar to the U.S. GAAP adopted by many foreign countries is the IFRS. Many foreign countries, including those of the European Union (EU), either require or allow IFRS for firms in their jurisdictions. The EU also accepts U.S. GAAP as equivalent to IFRS.

¹⁹ There are specific requirements that must be met to qualify as an FPI. Generally, an FPI could be any company that is registered in a foreign country but wishes to participate in U.S. capital markets. A foreign company may qualify as a foreign private issuer if 50% or less of its outstanding voting securities are held by U.S. residents if certain other conditions are met. A company may still qualify as an FPI even if more than 50% of voting securities are held by U.S. residents if certain other conditions are met. SEC, "Accessing the U.S. Capital Markets—A Brief Overview for Foreign Private Issuers," October 16, 2014, <https://www.sec.gov/divisions/corpfin/internatl/foreign-private-issuers-overview.shtml#I>.

domestic companies are not competitively disadvantaged with respect to regulatory requirements.... The first step in striking this balance is to determine which foreign companies should qualify as foreign private issuers and be able to avail themselves to the accommodations that go with that status.²⁰

Although the FASB and IFRS have pursued convergence of the accounting standards in the early 2000s, due to differences in the underlying approach, the two standard-setting bodies are, arguably, not actively pursuing convergence of the two standards.²¹ Some in the financial industry continue to advocate for the convergence of the two standards.²²

The older and more mature U.S. GAAP is considered a rules-based approach to standard-setting for the largest capital market in the world, where as the newer IFRS is considered a principles-based approach to standard-setting that is meant to be adoptable by developed and emerging economies.²³

Foreign firms that participate in the U.S. capital markets are required to file reports similar to domestic companies, even while they maintain their own domestic standards. A few of the common forms used by foreign firms are 20-F and 40-F (for Canadian firms) instead of 10-K and 6-K instead 8-K.²⁴

Annual Report to Shareholders

The annual report to shareholders—which is distinct from Form 10-K—is considered a state-of-the-company report to its shareholders and potentially interested stakeholders. It usually contains a letter from the CEO, financial data, results of operations, market segment information, new product plans, subsidiary activities, and information on research and development on future programs. The SEC requires the annual report to be sent to shareholders. The SEC also requires listed companies to post their annual reports and proxy materials on their websites.²⁵

The annual report filed with the SEC on Form 10-K might contain more detailed information about the company's financial condition than the annual report to shareholders does. A company may send its annual 10-K report to shareholders instead of creating a separate annual report. Registered FPIs are required to follow a similar set of requirements.

Proxy Statements

Proxy statements provide a firm's shareholders with information on substantive issues related to the firm. The SEC requires proxy statements, such as DEF 14A, to be provided to shareholders

²⁰ SEC, "SEC Solicits Public Comment on the Foreign Private Issuer Definition," press release, June 4, 2025, <https://www.sec.gov/newsroom/press-releases/2025-82-sec-solicits-public-comment-foreign-private-issuer-definition>.

²¹ SEC, "Spotlight on Work Plan for Global Accounting Standards," July 15, 2019, <https://www.sec.gov/spotlight/globalaccountingstandards.shtml>.

²² Matthew Winters, "CFA Institute Is Not Giving Up on the Convergence of GAAP and IFRS," CFA Institute, August 13, 2024, <https://blogs.cfainstitute.org/marketintegrity/2024/08/13/cfa-institute-is-not-giving-up-on-the-convergence-of-gaap-and-ifs/>.

²³ Stefan F. Schantl and Alfred Wagenhofer, "Principles-Based versus Rules-Based Accounting Standards: A Relevance-Enforceability Tradeoff," Columbia Business School, April 11, 2021, https://business.columbia.edu/sites/default/files-efs/imce-uploads/CEASA/Events%20Page/principles-based_versus_rules-based_accounting_standards.pdf.

²⁴ SEC, "Financial Reporting Manual: Topic 6—Foreign Private Issuers and Foreign Businesses," November 18, 2020, <https://www.sec.gov/about/divisions-offices/division-corporation-finance/financial-reporting-manual/frm-topic-6>.

²⁵ SEC, "Exchange Act Reporting and Registration," November 12, 2024, <https://www.sec.gov/resources-small-businesses/going-public/exchange-act-reporting-registration>.

before the company's annual meeting. It provides an avenue for the shareholders to influence the decisions of the firm's board of directors and management, including the selection of the board and compensation of company executives.²⁶ Compensation information for the top five compensated officers must include salary, bonuses, non-equity compensation, stock awards, options, and deferred compensation.²⁷

Regulation S-K

Regulation S-K provides a framework for sharing nonfinancial information with investors, the public, and the SEC. The regulation was adopted under the Securities Act of 1933 and the Securities Exchange Act of 1934 to create a uniform and integrated reporting framework for SEC-registered companies. Regulation S-K may require a firm to file certain forms with the SEC, such as the following:

- Form S-1: used by companies to register securities with the SEC.
- Form 10-K, 20-F for most foreign private issuers, or Form 40-F for Canadian firms: required annual financial report.
- Form 8-K or 6-K for all foreign firms: used to notify investors and the public of specific material events at a company.
- Proxy statement (e.g., DEF 14A): provides shareholders an avenue to influence corporate decisions, including compensation and who is on the board of directors. DEF 14A refers to final proxy statement, while 14A refers to proxy statements as required by Section 14(a) of the Securities and Exchange Act of 1934.²⁸

Auditing

Private or public sector stakeholders need to have reasonable assurance that the financial statements of an entity are free of material misstatement, whether caused by error or fraud.²⁹ In the private sector, independent assurance is provided by a qualified external party—an auditor. The auditor is engaged to give an unbiased professional opinion on whether the financial statements and related disclosures are fairly stated in all material³⁰ respects for a given period of time in accordance with GAAP.³¹

As a consequence of high-profile instances of financial accounting fraud in the early 2000s, Congress created the PCAOB as a nonprofit corporation to provide independent oversight of audits of public companies. The PCAOB also oversees the audits of brokers and dealers, including compliance reports.³² As a requirement of SOX, public accounting firms are required to register with the PCAOB to prepare or issue audit reports for companies listed in the United

²⁶ SEC, "Annual Meeting and Proxy Requirements," June 6, 2024, <https://www.sec.gov/resources-small-businesses/going-public/annual-meetings-proxy-requirements>.

²⁷ Georgetown Law Library, "Company Research Guide: Annual and Quarterly Reports and Proxy Statements," April 9, 2025, <https://guides.ll.georgetown.edu/companyresearch/annual-reports#>.

²⁸ SEC, "Proxy Statements: How to Find," <https://www.investor.gov/introduction-investing/investing-basics/glossary/proxy-statements-how-find>.

²⁹ PCAOB, "Auditing Standard No. 16: Matters Included in the Audit Engagement Letter," http://pcaobus.org/Standards/Auditing/Pages/Auditing_Standard_16_Appendix_C.aspx.

³⁰ *Material misstatement* in financial reporting can be defined as information that could potentially affect the investment decision or the conclusions drawn by a reader about the financial status of the firm. SEC, "SEC Staff Accounting Bulletin: No. 99 Materiality," August 13, 1999, <https://www.sec.gov/interp/account/sab99.htm#foot6>.

³¹ There are different types of audits and reviews beyond financial statement audits, such as financial reviews, operational audits, department reviews, information systems audits, integrated audits, investigative audits or reviews, forensic audits, tax audits, environmental and social impact audits, compliance audits, and follow-up audits.

³² PCAOB, "Mission and Vision," <https://pcaobus.org/About/History/Pages/default.aspx>.

States or broker-dealers or to play a substantial role in the audits of these firms.³³ PCAOB maintains a list of firms registered with the PCAOB.³⁴

The five board members of the PCAOB are appointed to staggered five-year terms by the SEC after consultation with the chairman of the Board of Governors of the Federal Reserve System and the Secretary of the Treasury. The SEC has oversight authority over the PCAOB, including the approval of the board's rules, standards, and budget.

PCAOB Funding

SOX was amended by the Dodd-Frank Act,³⁵ which established funding for the PCAOB's activities, primarily through the annual accounting support fees assessed on public companies and other issuers, as well as brokers and dealers registered with the SEC.³⁶ The PCAOB's budget for 2025 was nearly \$400 million. Approximately \$346 million of the accounting support fees to be collected will be allocated to public companies and \$29 million to brokers and dealers.³⁷ The difference in budgeted amount and collected fees are a consequence of amounts carried to 2025 from prior year.

Along with the creation of PCAOB, Section 404 of SOX also requires a public company's annual report to include the company's own assessment of internal control over financial reporting and an auditor's attestation (audit).³⁸ The different types of audit opinions an auditor may issue are discussed next, followed by a discussion of internal control integrated frameworks.

Audit Opinions

Auditors form audit opinions by examining the types of risks organizations might face and the types of controls that exist to mitigate those risks. Once the risks and controls to mitigate those risks have been determined, the auditors will examine the supporting evidence and determine if management is presenting the financial statements fairly in all material respects.³⁹ Although most entities will usually receive unqualified opinions, auditors may express other types of opinions based on the circumstances. There are four different types of audit opinions an auditor may express:⁴⁰

1. **Unqualified opinion.** An unqualified opinion states that the financial statements present fairly, in all material respects, the financial position, results of operations, and cash flows of the entity in conformity with GAAP. This is the opinion expressed in the standard report. Under certain circumstances, explanatory language might be added to the auditor's standard report while not affecting the auditor's unqualified opinion on the financial statements.
2. **Qualified opinion.** A qualified opinion states that, except for the effects of the matter(s) to which the qualification relates, the financial statements present fairly

³³ PCAOB, "Registration," <https://pcaobus.org/oversight/registration>.

³⁴ PCAOB, "Registered Firms," <https://pcaobus.org/oversight/registration/registered-firms?pg=6>.

³⁵ P.L. 111-203.

³⁶ 15 U.S.C. §7219. PCAOB, "About the PCAOB," <https://pcaobus.org/About/Pages/default.aspx>.

³⁷ PCAOB, "2025 Budget by Cost Category," https://assets.pcaobus.org/pcaob-dev/docs/default-source/about/administration/documents/fiscal_year_budgets/1a-2025-budget—public-budget.pdf.

³⁸ 15 U.S.C. §78m and 15 U.S.C. §78o(d).

³⁹ PWC, "What Is an Audit?," <http://www.pwc.com/m1/en/services/assurance/what-is-an-audit.html>.

⁴⁰ Public Company Accounting Oversight Board, *AS 3100: Reports on Audited Financial Statements*, <https://pcaobus.org/Standards/Auditing/Pages/AS3101.aspx>.

in all material respects the financial position, results of operations, and cash flows in conformity with GAAP.

3. **Adverse opinion.** An adverse opinion states that the financial statements do not present fairly the financial position, results of operations, or cash flows of the entity in conformity with GAAP.
4. **Disclaimer of opinion.** A disclaimer of opinion states that the auditor does not express an opinion on the financial statements. This option may indicate that the auditor does not think there is enough information to form a conclusive opinion.

Limits of Audit

Independent audit opinions do not fully guarantee that financial statements are presented fairly in all material respects for the following key reasons:

- Auditors generally use statistical methods for random sampling and look at only a fraction of the economic events or documents during audits. It is cost- and time-prohibitive to recreate or include in a sample all economic events at an entity.
- Frequently many line items on the financial statements involve subjective decisions or a degree of uncertainty as a result of using estimates.
- Audit procedures cannot eliminate potential fraud by management, though it is possible an auditor may find fraud committed by management during the audit process.

Thus, the auditor provides only a *reasonable* assurance about whether the financial statements are free of material misstatement.

Going forward, the use of artificial intelligence (AI) or other machine learning tools potentially expands the amount of information that an auditor may consider, which could help improve audit quality. Improved audit procedures could help the management of the audited firm issue more accurate financial reports. As one author argued:

AI can be used in a variety of ways, including performing journal entry testing by identifying unusual transactions among a large pool of unstructured data and analyzing those transactions for patterns and anomalies. AI can also be used in the audit's planning phase and when performing risk identification and assessment procedures. AI can process large amounts of data (such as reading bank statements and legal contracts) and reconcile accounts many times faster than a human auditor can—and with fewer errors. Using AI-powered technology tools, the auditor can move beyond traditional practices to more efficiently analyze client information and more easily identify risk, thereby enhancing audit quality.⁴¹

Limits of Auditors

Sometimes, stakeholders assume that auditors are responsible for various functions of the company or the management, including the issuance of the financial report. As previously discussed, auditors do not look at every transaction. Similarly, they do not check all figures in financial reports or test the adequacy of all internal controls. (see “COSO Framework” below).

⁴¹ Anita Dennis, “What AI Can Do for Auditors,” *Journal of Accountancy*, February 1, 2024, <https://www.journalofaccountancy.com/issues/2024/feb/what-ai-can-do-for-auditors/>.

While auditors, usually, have a degree of knowledge about the businesses they are auditing, they are not hired to render opinions on the business activities or strategies undertaken by company management. Similarly, they are not hired to issue opinions on the quality of management.⁴²

An audit also cannot provide a guarantee that the business will continue in business, nor is an auditor on-site all the time with the audit client. Auditors substantially rely on the information provided by company management.⁴³

COSO Framework

Section 404 of SOX requires management at a public company to select an internal control framework and then assess and report annually on the design and operating effectiveness of the internal controls. The internal control framework widely used by the business community is the one created by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.⁴⁴ COSO's mission is to help organizations improve performance by enhancing internal control, risk management, governance and fraud deterrence.⁴⁵

SEC Internal Control: Integrated Framework Requirements

SOX required the SEC to require a public company's annual report to contain (1) a statement of management's responsibility for establishing and maintaining an adequate internal control structure and procedures and (2) management's assessment of the internal control structure and procedures for financial reporting. Under the SEC's final rules, an annual report on internal control is required to contain:

- a statement of management's responsibility for establishing and maintaining adequate internal control over financial reporting for the company,
- a statement identifying the framework used by management to evaluate the effectiveness of this internal control,
- management's assessment of the effectiveness of this internal control as of the end of the company's most recent fiscal year, and
- a statement that its auditor has issued an attestation report on management's assessment.

The business community created the COSO framework to meet the above requirements.

Internal control helps entities achieve important objectives and sustain and improve performance. Entities, whether private or public, use internal controls to achieve their objectives by designing processes that control organizational risk. An effective internal control framework requires an entity's management and board of directors to use judgment that is dynamic, integrated, and responsive to the needs of the company⁴⁶ rather than rigidly adhere to past policies and procedures.

A COSO framework, depicted in **Figure 3**, was created to help practitioners assess internal controls not as an isolated issue but rather as an integrated framework for how internal controls work together across an organization to help achieve the objectives as determined by management.

⁴² PWC, "What Is an Audit?"

⁴³ PWC, "What Is an Audit?"

⁴⁴ There are five private sector entities that support COSO: the American Accounting Association, the Financial Executives International, the Association of International Certified Public Accountants, the Institute of Internal Auditors, and the Association of Accountants and Financial Professionals in Business.

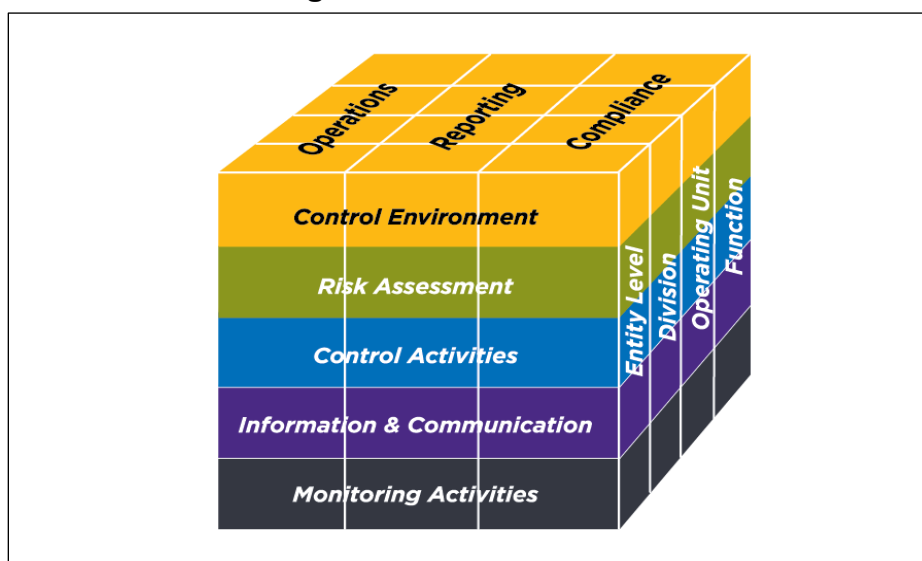
⁴⁵ COSO, "About Us," <https://www.coso.org/about-us>.

⁴⁶ KPMG, "COSO Internal Control—Integrated Framework (2013)," <https://assets.kpmg.com/content/dam/kpmg/pdf/2016/05/2750-New-COSO-2013-Framework-WHITEPAPER-V4.pdf>.

The cube in **Figure 3** represents the integrated perspective recommended by COSO for practitioners who are creating and assessing internal controls. The cube may be best understood by examining each set of components separately:

- The three objectives—Operations, Reporting, and Compliance—are represented by the columns. The objectives are designed to help an organization focus on different aspects of internal control to help management achieve its objectives.
- The five components—Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring Activities—are represented by the rows. The components represent what is required to achieve the three objectives.
- An entity’s organizational structure—Entity-Level, Division, Operating Unit, and Function—is represented by the third dimension. For an organization to achieve its objectives, according to COSO, internal control must be effective and integrated across all organization levels.⁴⁷

Figure 3. COSO Framework



Source: COSO, “Leveraging COSO Across the Three Lines of Defense,” July 2015, p. 1, https://www.coso.org/_files/ugd/3059fc_cc80a9492ca743fd90d517049736c4da.pdf.

Policy Issues

Through hearings, Member statements, and (periodically) legislation, Congress weighs in on matters related to public company financial reporting and auditing and generally implements policy through and exercises oversight of the various agencies and organizations mentioned above. As discussed, Congress has given the SEC the authority to determine the appropriate financial reporting and auditing standards in the United States for the private sector while maintaining its oversight authority. For financial reporting, the SEC recognizes the FASB as the designated organization for establishing GAAP. Congress created the PCAOB to provide independent oversight of audits of public companies.

⁴⁷ COSO, “Leveraging COSO Across the Three Lines of Defense,” July 2015, https://www.coso.org/_files/ugd/3059fc_cc80a9492ca743fd90d517049736c4da.pdf.

A few of the more recent issues that could be of interest to Congress are highlighted below.

Accounting for Crypto Assets

In early 2025, the SEC issued Staff Accounting Bulletin (SAB) 122 to rescind SAB 121, *Accounting for Obligations to Safeguard Crypto-Assets an Entity Holds for Its Platform Users*.⁴⁸ SAB 121 was issued on March 31, 2022, and went into effect for annual reporting periods beginning after December 15, 2024, with early adoption permitted.

After SAB 121 was issued, a number of Members and industry proponents asserted that it deviated from established accounting standards by requiring a custodian to recognize a liability and hold a corresponding offset on the balance sheet measured at fair value and that it failed to accurately reflect the underlying legal and economic obligations of the custodian. In addition, critics of SAB 121 argued that this staff guidance should have been issued through the rulemaking process subject to the requirements of the Administrative Procedure Act (P.L. 79-404).⁴⁹

SAB 122 rescinding SAB 121 became effective January 30, 2025. Thus, SAB 121 was in effect for a little more than a month, and its requirements would generally have had minimal reporting impact, but it is possible that some firms may have made significant efforts to become compliant with SAB 121 for the upcoming annual reporting period. According to SAB 122 Supplementary Information:

The statements in staff accounting bulletins are not rules or interpretations of the Commission, nor are they published as bearing the Commission’s official approval. They represent interpretations and practices followed by the Division of Corporation Finance and the Office of the Chief Accountant in administering the disclosure requirements of the Federal securities laws.⁵⁰

While SABs are not on the same level as FASB GAAP requirements in the accounting hierarchy⁵¹, the Government Accountability Office noted that SABs can change firms’ expectations of how the SEC will evaluate their compliance with disclosure requirements.⁵²

SAB 121 Requirements

SAB 121 sought to establish financial reporting requirements for crypto assets that are safeguarded by an entity on behalf of another.⁵³ When SAB 121 was issued, the SEC identified

⁴⁸ SEC, Staff Accounting Bulletin No. 121, March 31, 2022, <https://www.sec.gov/rules-regulations/staff-guidance/staff-accounting-bulletins/staff-accounting-bulletin-121>.

⁴⁹ House Committee on Financial Services, “McHenry, Lummis Demand SEC Rescind SAB 121 Amid Bipartisan, Bicameral Opposition,” press release, September 23, 2024, <https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=409387>.

⁵⁰ SEC, Staff Accounting Bulletin No. 122, January 23, 2025, <https://www.sec.gov/rules-regulations/staff-guidance/staff-accounting-bulletins/staff-accounting-bulletin-122>.

⁵¹ Corporate Finance Institute, “GAAP Hierarchy,” <https://corporatefinanceinstitute.com/resources/accounting/gaap-hierarchy/>.

⁵² Edda Emmanuelli Perez, “Decision: Securities and Exchange Commission—Applicability of the Congressional Review Act to Staff Accounting Bulletin No. 121,” Government Accountability Office, October 31, 2023, <https://www.gao.gov/assets/870/862501.pdf>.

⁵³ For more information on crypto assets, see CRS Report R47425, *Cryptocurrency: Selected Policy Issues*, by Paul Tierno; CRS In Focus IF12984, *Key Issues in Stablecoin Legislation in the 119th Congress*, by Paul Tierno and Marc Labonte; and CRS Insight IN12358, *Potential Disapproval of SEC Staff Accounting Bulletin No. 121 Under the Congressional Review Act*, by Maeve P. Carey, Andrew P. Scott, and Paul Tierno.

that the custodial relationships related to the unique technological, legal, and regulatory risks of crypto assets are different than those of other custodial relationships. SAB 121 did not define *safeguarding*, and it was left up to the entities to determine whether a transaction was within the scope of SAB 121.⁵⁴

An entity, generally, does not record its custodial assets as belonging to the entity—therefore, it would not be recorded as an asset on its balance sheet. SAB 121 required the entity holding the custodial asset to record a liability and corresponding asset based on fair value.⁵⁵ FASB’s Topic 820 defines *fair value* as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.”⁵⁶ *Market participants* is defined as buyers and sellers that are (1) not related parties, (2) knowledgeable about the asset or liability and the transaction, and (3) willing and able to enter into the transaction. In simpler terms, fair value might be described as how much someone who is not influenced by any other incentives is willing to pay for an asset or receive for a liability. Alternatively, it is the entry or exit price at which a willing buyer and seller would agree to exchange an asset or liability.⁵⁷

SAB 121 also required a custodian of crypto assets to disclose:

- detailed information about the nature and amount of crypto assets held,
- vulnerabilities related to concentration,
- who holds the cryptographic keys,
- who maintains internal recordkeeping, and
- who is obligated to secure and protect the assets from loss or theft.

SAB 122 Rescission of SAB 121

SAB 122 requires full retrospective application and derecognition of changes required by SAB 121 for annual periods beginning after December 15, 2024. For any entities that had adopted SAB 121, they are given the option to apply SAB 122 to any earlier interim or annual financial statement period.

If an entity chooses to retrospectively apply SAB 122, it is required to adjust the prior financial statements by eliminating the recording of custodial assets and liabilities.⁵⁸ Also, an entity should make other adjustments to the financial statements as necessary to undo any prior effect on the financial statement of the custodial entity.

SAB 122 requires a custodian of crypto assets to determine whether a liability related to the risk of loss exists.⁵⁹ If such a liability exists, U.S. GAAP requires an entity to record an accrual for a loss contingency when:

⁵⁴ Deloitte, “SAB 121 and Done: SEC Issues SAB 122 to Rescind Guidance on Safeguarding Crypto Assets,” January 27, 2025, <https://dart.deloitte.com/USDART/home/publications/deloitte/heads-up/2025/sec-rescinds-sab-121-issues-sab-122-crypto-cryptocurrency>.

⁵⁵ For more detailed discussion of fair value, See Appendix B in CRS Report R44193, *Federal Credit Programs: Comparing Fair Value and the Federal Credit Reform Act (FCRA)*, by Raj Gnanarajah.

⁵⁶ FASB, “Fair Value Measurement (Topic 820),” <https://asc.fasb.org/820/showallinonepage>.

⁵⁷ Anthony Curcio and Roger Von Elm, “Fair Value in Federal Credit,” Summit, March 12, 2025, <https://www.summitllc.us/blog/fair-value-accounting-federal-creditwhite-paper>.

⁵⁸ KPMG, “SEC Rescinds SAB 121,” January 2025, <https://kpmg.com/us/en/frv/reference-library/2025/sec-rescinds-sab-121.html>.

⁵⁹ SEC, Staff Accounting Bulletin No. 122.

- it is probable a loss has been incurred and
- the amount can be reasonably estimated.⁶⁰

An entity that is not expected to incur a loss would not be required to record a liability under SAB 122. SAB 122 included a reminder that an entity should continue to take into consideration existing disclosure requirements that allow investors to understand an entity's obligation to safeguard crypto assets held for others.

Some have stated that SAB 122 does not change the requirement for an entity that is safeguarding digital assets to have others determine if the entity controls the assets. In such instances, the entity would be required to record the related asset and liability to reflect its obligation to return those digital assets to their legal owner on its balance sheet.⁶¹

The Digital Asset Market Clarity Act of 2025 (H.R. 3633)

The House passed the Digital Asset Market Clarity Act of 2025 (H.R. 3633) in July 2025. Section 310 of the bill would stipulate that a federal banking agency, the National Credit Union Administration, or the SEC may not require financial institutions to treat assets held in custody as liabilities on the financial statement or their balance sheets. The act would also generally prevent those financial regulators from requiring custodians of digital assets to hold regulatory capital against operations risks. Also, the bill would require that a liability cannot be recorded for any obligation that an entity does not own if that liability will exceed the expense recognized on the income statement—in other words, it would prevent a liability from being recorded on the balance sheet.

PCAOB and Foreign Audit Firms

Foreign firms accessing U.S. capital markets use foreign auditors from their home countries to audit their financial records. Over the past two decades, the PCAOB has entered into agreements with more than 50 foreign regulators.⁶² Similar to the access PCAOB has with audit firms based in the United States, these agreements exist to give the PCAOB access to foreign audit firms' work papers. While many of these cooperative agreements are made public, agreements with select countries—including Australia, Canada, China, Singapore, and South Korea—have not been made public. Despite these agreements, the PCAOB has faced restrictions on its ability to examine foreign firms' audit work papers in the People's Republic of China,⁶³ including Hong Kong.⁶⁴

Congress passed the Holding Foreign Companies Accountable Act (HFCAA, P.L. 116-222) to address audit limitations faced by the PCAOB. HFCAA requires foreign companies listed in U.S. stock exchanges to be subject to the same accounting and audit oversight as listed domestic

⁶⁰ Deloitte, "SAB 121 and Done."

⁶¹ KPMG, "SEC Rescinds SAB 121."

⁶² PCAOB, "PCAOB Cooperative Arrangements with Non-U.S. Regulators," <https://pcaobus.org/oversight/international>.

⁶³ For more back ground on this issue, see CRS In Focus IF12212, *U.S.-China Auditing Agreement and Issues for Congress*, by Karen M. Sutter, Michael D. Sutherland, and Raj Gnanarajah.

⁶⁴ House Committee on Oversight and Government Reform, "Comer Opens Inquiry into PCAOB Oversight of Audits for China-Based Companies," press release, March 13, 2024, <https://oversight.house.gov/release/comer-opens-inquiry-into-pcaob-oversight-of-audits-for-china-based-companies/>.

companies. The law requires the SEC to identify each foreign firm not in compliance and suspend trading of those companies from U.S. exchanges after three years of noncompliance.

As a consequence of the HFCAA requirements, the PCAOB and Chinese financial authorities agreed on a new Statement of Protocol in 2022.⁶⁵ The PCAOB is expected to periodically reassess the effectiveness of the new protocol.

The Statement of Protocol includes commitment from Chinese authorities on four issues:

1. **Engagement Selection:** PCAOB has discretion to select audit firms and clients that it examines.
2. **No Redaction:** PCAOB can see all audit work papers without any redactions. For restricted data, including personally identifiable information, there are specific processes for viewing.
3. **Testimony:** PCAOB can interview and obtain testimony from audit firm personnel in China and Hong Kong.
4. **Onward Sharing:** Information, including restricted data, can be shared with the SEC for all purposes, including administrative and civil enforcements.⁶⁶

Meanwhile, according to the U.S.-China Economic and Security Review Commission, as of March 7, 2025, U.S. exchanges list 286 Chinese companies with \$1.1 trillion in total market capitalization. Since January 2024, 48 Chinese companies have listed on the three U.S. exchanges, raising \$2.1 billion in combined initial public offerings.⁶⁷

Transferring PCAOB Functions to the SEC

Before the enactment of the FY2025 reconciliation act in P.L. 119-21, earlier versions of H.R. 1 (then-named the One Big Beautiful Bill Act) had included provisions that would have transferred the functions of the PCAOB to the SEC. One of these provisions was Section 50002 of a June 2025 House-passed version of H.R. 1.

The Senate Committee on Banking, Housing, and Urban Affairs released a similar legislative proposal but with some differences.⁶⁸ According to Senator Warren,⁶⁹ the Senate Parliamentarian determined that this provision violated the Byrd rule.⁷⁰ The provision was not included in the enacted version.

⁶⁵ PCAOB, “PCAOB Signs Agreement with Chinese Authorities, Taking First Step Toward Complete Access for PCAOB to Select, Inspect and Investigate in China,” press release, August 26, 2022, <https://pcaobus.org/news-events/news-releases/news-release-detail/pcaob-signs-agreement-with-chinese-authorities-taking-first-step-toward-complete-access-for-pcaob-to-select-inspect-and-investigate-in-china>.

⁶⁶ SEC, *PCAOB Agreement with China on Audit Inspections and Investigations*, <https://www.sec.gov/files/china-sop-fact-sheet.pdf>.

⁶⁷ U.S. China Economic and Security Review Commission, *Chinese Companies Listed on Major U.S. Stock Exchanges*, March 7, 2025, p. 1, https://www.uscc.gov/sites/default/files/2025-03/Chinese_Companies_Listed_on_US_Stock_Exchanges_03_2025.pdf.

⁶⁸ The committee’s proposal can be found at https://www.banking.senate.gov/imo/media/doc/obbb_-_banking_textpdf.pdf.

⁶⁹ Committee on Banking, Housing, and Urban Affairs, “Statement by Senator Warren on Senate Parliamentarian Advising on Republican Provisions in Budget Bill,” press release, June 20, 2025, <https://www.banking.senate.gov/newsroom/minority/statement-by-senator-warren-on-senate-parliamentarian-advising-on-republican-provisions-in-budget-bill>.

⁷⁰ For more detailed information on the Byrd rule, see, CRS Report RL30862, *The Budget Reconciliation Process: The Senate’s “Byrd Rule”*, by Bill Heniff Jr.

The PCAOB's budget for 2025 is \$399.7 million. It is primarily funded through fees assessed on the private entities it oversees. SEC funding is provided by the Financial Services and General Government bill and is offset through fees collected by the SEC. Section 50002 would have transferred all unobligated fees collected by the PCAOB to the Treasury General Fund and remove the PCAOB funding authority as provided in SOX. Shifting PCAOB-related spending to the SEC would decrease the deficit by \$771 million over 10 years because, according to scoring conventions, future SEC appropriations and offsetting collections are not included in this score. Any future budgetary effects of these changes would depend on what spending levels are approved for PCAOB-related functions in future appropriations for the SEC.

An earlier House-passed version of H.R. 1 would have required the PCAOB to share with the SEC any intellectual property related to its programs. This proposal would have transferred duties and powers of the PCAOB, along with all existing processes and regulations, to the SEC and leave them in effect unless modified by the SEC through rulemaking. The transfer would also include all auditing standards currently established by the PCAOB. Pending enforcement and disciplinary action of the PCAOB would be transferred to the SEC or other regulators as required by law.⁷¹

The proposal would have allowed the SEC to offer PCAOB employees equivalent positions at the SEC subject to SEC's standard employment policies and receive pay that is not higher than the highest paid employee of similarly situated employee of the commission. It would have also prohibited the SEC from using its funds to carry out the functions of the PCAOB, as PCAOB would arguably cease to exist, and the functions of PCAOB would be integrated into the SEC. Thus, there would not be a need to carry out the functions of the PCAOB separately.

In April 2025, the PCAOB chair stated that, should PCAOB functions be transferred to the SEC, the current inspections could be disrupted while a new program is setup within the SEC. The chair also indicated that its international cooperative agreements do not contain provisions that would allow the PCAOB's privileges and responsibilities to be transferred to the SEC and would need to be renegotiated.⁷²

With respect to China, the chair stated:

The PCAOB secured every concession we demanded from China in the Statement of Protocol that facilitates our access to inspect and investigate completely. We have their feet to the fire. Scrapping that agreement and starting over gives China the opportunity to exploit the uncertainty in order to avoid scrutiny of its audit work once again, to the detriment of investors.⁷³

⁷¹ 15 U.S.C. §7215.

⁷² Erica Y. Williams, PCAOB, "PCAOB Chair Williams Delivers Remarks at the Investor Advisory Group Meeting," April 29, 2025, <https://pcaobus.org/news-events/speeches/speech-detail/pcaob-chair-williams-delivers-remarks-at-the-investor-advisory-group-meeting>.

⁷³ Williams, "PCAOB Chair Williams Delivers Remarks."

Appendix A. Glossary of Financial Statements

Appendix B provides a description of the financial statements listed in **Table 1** and **Table A-1** by each sector.

Table A-1. Comparison of Financial Statements in Various Sectors

Private Sector ^a	Federal Government ^b	State and Local Governments ^c
Income Statement	Statement of Operations and Changes in Net Position	Statement of Activities
Balance Sheet	Balance Sheet	Statement of Net Position (Assets)
Statement of Shareholders' Equity	Statement of Operations and Changes in Net Position	Statement of Net Position (Assets)
Statement of Cash Flows	Statement of Changes in Cash Balance from Unified Budget and Other Activities	Statement of Activities
Not Applicable	Statement of Net Cost	Required Supplementary Information
Not Applicable	Reconciliations of Net Operating Cost and Unified Budget Surplus (Deficit)	Required Supplementary Information
Not Applicable	Statement of Social Insurance	Required Supplementary Information
Notes to the Financial Statements	Notes to the Financial Statements	Notes to the Financial Statements
Management's Discussion and Analysis of Financial Condition and Results of Operation ^d	Management's Discussion and Analysis	Management's Discussion and Analysis
Management's Discussion and Analysis of Financial Condition and Results of Operation	Understanding the Financial Report of the United States Government ^e	Letter of Transmittal
Management's Discussion and Analysis of Financial Condition and Results of Operation	Required Supplementary Information	Required Supplementary Information
Management's Discussion and Analysis of Financial Condition and Results of Operation	Budget of the U.S. Government ^f	Statistical Section

Source: CRS.

Notes:

- a. Many of the financial statements in the government sector do not exist in the private sector or are not relevant.
- b. The financial statements listed below are from the *Financial Report of the United States Government: Fiscal Year 2024*. The financial statements listed in **Table 1** provide a comparison to the private sector. Individual agency financial reports may differ based on their function and purpose from what is listed for the federal government. See Department of the Treasury, *Financial Report of the United States Government: Fiscal Year 2024*, January 16, 2025, [https://www.fiscal.treasury.gov/files/reports-statements/financial-report/2024/01-16-2025-FR-\(Final\).pdf](https://www.fiscal.treasury.gov/files/reports-statements/financial-report/2024/01-16-2025-FR-(Final).pdf).
- c. The financial statements listed below are from the Annual Comprehensive Financial Report of the State of Ohio. Other states' and territories' financial statements might differ due to their respective laws and requirements. Only government-wide financial statements are included, and specific fund financial statements—such as proprietary funds, fiduciary funds, and fiduciary component units—are not listed. See

- State of Ohio, *State of Ohio: Annual Comprehensive Financial Report: Fiscal Year Ended June 30, 2024*, December 18, 2024, https://archives.obm.ohio.gov/Files/State_Accounting/Financial_Reporting/Comprehensive_Annual_Financial_Report/2024/ACFR_2024.pdf.
- d. Some elements of the various statements and schedules in the government sector might be similar in the management's discussion and analysis of financial condition and results of operation in the private sector, but most elements are not relevant or are not presented.
 - e. U.S. Government Accountability Office, *Understanding the Financial Report of the United States Government*, GAO-18-239SP, February 15, 2018, <https://www.gao.gov/products/gao-18-239sp>.
 - f. For the purpose of this table, the federal budget includes all supporting schedules. See Office of Management and Budget, "President's Budget," <https://www.whitehouse.gov/omb/information-resources/budget/>.

Private Sector

The **income statement** presents the results of a company's operations and whether it was profitable or incurred a loss during the period measured. Publicly traded companies issue income statements quarterly and annually, along with other financial statements.

The **balance sheet** presents a company's financial position at the end of a specified period. The balance sheet summarizes assets, liabilities, and sometimes owners' equity. Publicly traded companies issue balance sheets quarterly and annually, along with other financial statements.

The **statement of shareholders' equity** presents the ownership interest of the shareholders in the company. For a sole proprietorship, a statement of owner's equity represents the owner's interest in the company after accounting for assets and liabilities. For publicly traded companies, statement of shareholders' equity will also present detailed information on the changes in each type of stockholder equity account (e.g., preferred stock, common stock, additional paid in capital, and retained earnings) during the period measured. Publicly traded companies issue statements of shareholders' equity quarterly and annually, along with other financial statements.

The **statement of cash flows** presents the cash generated and used during the period. Statement of cash flows is often divided into three separate components: operations, investing, and financing. Publicly traded companies issue statements of cash flows quarterly and annually, along with other financial statements.

The **notes to the financial statements** provide additional information to the financial statements and are often longer than the financial statements. The notes are an integral part of financial statements, and they provide information about assumptions and methodologies and other critical information necessary to understand the financial statements.

The **management's discussion and analysis of financial condition and results of operation (MD&A)** provides management's overview of the company's past performance and projections of future performance. The discussion and analysis could include growth and strategy, challenges and opportunities, market conditions, and market share. MD&A is not audited by an independent auditor; it represents the thoughts and opinions of management. MD&A is included in the annual report Form 10-K that is filed with the SEC and is also part of the annual report to shareholders.

Federal Government⁷⁴

The **statement of operations and changes in net position** presents the accrual-based results of the federal government's operations. It also shows how net operating revenue affects the

⁷⁴ Government Accountability Office, *Understanding the Financial Report of the United States Government*, GAO-18-239SP, February 2018, <https://www.gao.gov/assets/700/690243.pdf>.

government's net financial position as of a given date—usually the end of the fiscal year (September 30 for the federal government).

The **balance sheet** presents the federal government's financial position at the end of the fiscal year (September 30). The balance sheet summarizes assets, liabilities, and net position. The net position on the balance sheet is the same as the net position reported in the statement of operations and changes in net position.

The **statement of changes in cash balance from unified budget and other activities** presents how the change in the balance of cash and other monetary assets affects the cash-based budget surplus or deficit. The statement begins with the cash-based budget surplus or deficit and shows the items that affected the government's budget. The statement provides an explanation of how the budget deficits were financed. A budget deficit is the result of outlays (expenditures) exceeding receipts (revenue).

The **statement of net cost** presents the annual costs to operate the federal government at the agency level. Costs and earned revenue presented in the financial report is on an accrual basis, while the budget statements present costs and revenues, generally on a cash basis.

The **reconciliation of net operating cost and unified budget surplus (deficit)** presents how the annual unified budget surplus (or deficit) relates to the change in the government's cash and other monetary assets, as well as debt held by the public. The statement begins with the net operating result (revenue or cost) from the statement of operations and changes in net position and presents the items that explain the difference between that amount and the federal government's annual cash-based deficit or surplus.

The **statement of social insurance** provides estimates of the most significant social insurance programs (e.g., Social Security and Medicare). The estimates are actuarial present values of the projections and are based on the economic and demographic assumptions representing the trustees' estimates.

The **notes to the financial statements** provide information about assumptions and methodologies and other critical information necessary to understand the financial statements. In the 2025 financial report of the U.S. government, the presentation of financial statements comprised 20 pages; the 24 notes to the financial statements comprised 88 pages.⁷⁵

The **executive summary** (previously “A Citizen's Guide”) provides a high-level summary of the U.S. government's current financial position and condition and highlights key financial topics, including fiscal sustainability.⁷⁶

The **management's discussion and analysis (MD&A)** provides management's perspective and analysis of information presented in the financial report to Congress and citizens in more detail than the executive summary. The discussion and analysis include a table of the audit opinions of the respective agencies of the federal government and an explanation of the accounting differences between the budget and the financial report.

The **required supplementary information** provides additional information to enhance understanding of the federal government's operations or financial condition. The topics discussed

⁷⁵ Department of the Treasury, *Financial Report of the United States Government FY 2024*, January 16, 2025, [https://www.fiscal.treasury.gov/files/reports-statements/financial-report/2024/01-16-2025-FR-\(Final\).pdf](https://www.fiscal.treasury.gov/files/reports-statements/financial-report/2024/01-16-2025-FR-(Final).pdf).

⁷⁶ Department of the Treasury, *Financial Report of the United States Government FY 2024*; and Department of the Treasury, *Financial Report of the U.S. Government FY 2016*, January 12, 2017, p. 2, https://www.fiscal.treasury.gov/fsreports/rpt/finrep/fr/fr_index.htm.

encompass a range of issues, such as the sustainability of Social Security and Medicare trust funds or the sustainability of fiscal policy, including the debt-to-GDP ratio.

The ***Budget of the U.S. Government*** contains many of the elements contained in the statistical section of the Annual Comprehensive Financial Report (ACFR).⁷⁷ It contains financial and narrative information of past performance and future expectations for up to 10 years. It provides detailed information about the economic assumptions and interactions with the budget, performance and management, budget concepts and budget process, federal receipts, special topics, and technical budget analyses.

State and Local Governments⁷⁸

The **statement of activities** presents the results of the state or local government's operations. It lists revenues and expenses or expenditures and calculates the differences between them—along with other changes that are not revenues, expenses, or expenditures—and presents the net assets.

The **statement of net position** presents the balance of the state or local government's net assets (the difference between assets and liabilities) at the end of the fiscal year. The change in net assets over time provides a measurement of how well the elected or appointed officials are managing the revenues and expenses of the government.

The **fund financial statements** include governmental funds, proprietary funds, fiduciary funds, fiduciary component units, and other schedules to enhance the understanding of the ACFR. The financial statements included in the fund financial statements might more closely align with private sector financial statements.

The **required supplementary information** provides additional information to enhance the understanding of the state or local government's operations or financial condition. The topics discussed encompass a range of issues, such as pension plans; status of highways, bridges, and public transportation; and certain financial statements that might either present or reconcile the budget with expenditures.

The **notes to the financial statements** provide information about assumptions and methodologies and other critical information necessary to understand the financial statements. Notes should also provide sufficient information to distinguish between the primary government and its component units.

The **letter of transmittal** provides a high-level summary of the state or local government's current financial position and condition and highlights key financial topics, including a discussion of the local economy, a discussion of the long-term goals and objectives of major programs and services (including capital projects), and a description of the policies and controls regarding cash and investments. It is complementary to the management's discussion and analysis.

The **management's discussion and analysis (MD&A)** provides management's perspective and analysis of information presented in the financial report to the state or local legislature and citizens. The discussion and analysis distinguish between the primary government and its component units. In addition to the state or local government's primary financial statements

⁷⁷ The ACFR is a way for governments to show how they collected and expended funds to benefit their citizenry. Government Finance Officers Association, "Popular Reporting of Financial Information," September 25, 2020, <https://www.gfoa.org/materials/popular-reporting-of-financial-information>.

⁷⁸ Governmental Accounting Standards Board, "Financial Reporting Codification: 2200 Annual Comprehensive Financial Report," <https://gars.gasb.org/3154072/2147483466>.

(government-wide financial statements), it might also include other fund financial statements, including proprietary funds, fiduciary funds, and fiduciary component units.

The **statistical section** provides users of the financial statements with additional historical perspective, context, and detail to enhance the understanding of an ACFR. It is usually presented in five categories: Financial Trends, Revenue Capacity, Debt Capacity, Demography and Economy, and Operating Information.

Appendix B. CPA Ethics

CPA licenses are granted by each state.⁷⁹ CPAs are subject to various ethical requirements, including mandatory ethics courses to renew the CPA license every three years. They are subject to discipline by various regulatory bodies and professional organizations if they violate ethical requirements. The PCAOB requires registered public accounting firms and their associated persons to comply with PCAOB ethics and independence rules and standards. In addition, the PCAOB has specific rules on independence, integrity, and objectivity for CPAs.⁸⁰

Underlying these requirements are professional expectations of CPAs by Congress and the public. As the auditors of public and private companies are paid by the clients they audit, there is a degree of skepticism about auditor independence.⁸¹ In addition to the requirements placed by the PCAOB on the accounting profession to address these concerns, there are various professional accounting bodies that create their own codes of conduct. Among these, one of the most widely recognized is the AICPA's Code of Professional Conduct. This section presents excerpts from that code of conduct and then concludes by discussing some of the tools available to discipline CPAs and other accounting professionals.

AICPA Principles of Professional Conduct⁸²

Preamble

Membership in the American Institute of Certified Public Accountants is voluntary. By accepting membership, a *member* assumes an obligation of self-discipline above and beyond the requirements of laws and regulations.

These Principles of the Code of Professional Conduct of the American Institute of Certified Public Accountants express the profession's recognition of its responsibilities to the public, to *clients*, and to colleagues. They guide *members* in the performance of their professional responsibilities and express the basic tenets of ethical and professional conduct. The Principles call for an unswerving commitment to honorable behavior, even at the sacrifice of personal advantage.

Responsibilities

Responsibilities principle. In carrying out their responsibilities as professionals, members should exercise sensitive professional and moral judgments in all their activities.

As professionals, members perform an essential role in society. Consistent with that role, members of the American Institute of Certified Public Accountants have responsibilities to all those who use their professional services. Members also have a continuing responsibility to cooperate with each other to improve the art of accounting, maintain the public's confidence, and carry out the profession's special responsibilities for self-governance. The collective efforts of all members are required to maintain and enhance the traditions of the profession.

⁷⁹ National Association of State Boards of Accountancy, "Boards of Accountancy," <https://nasba.org/stateboards/>.

⁸⁰ PCAOB, "Ethics and Independence," <https://pcaobus.org/oversight/standards/ethics-independence-rules>.

⁸¹ SEC, "SEC Updates Auditor Independence Rules," press release, October 16, 2020, <https://www.sec.gov/newsroom/press-releases/2020-261>.

⁸² AICPA, "AICPA Code of Professional Conduct," March 2025, <https://www.aicpa-cima.com/membership/landing/aicpa-membership-requirements>.

The Public Interest

The public interest principle. Members should accept the obligation to act in a way that will serve the public interest, honor the public trust, and demonstrate a commitment to professionalism.

A distinguishing mark of a profession is acceptance of its responsibility to the public. The accounting profession's public consists of clients, credit grantors, governments, employers, investors, the business and financial community, and others who rely on the objectivity and integrity of members to maintain the orderly functioning of commerce. This reliance imposes a public interest responsibility on members. The public interest is defined as the collective well-being of the community of people and institutions that the profession serves.

In discharging their professional responsibilities, members may encounter conflicting pressures from each of those groups. In resolving those conflicts, members should act with integrity, guided by the precept that when members fulfill their responsibility to the public, clients' and employers' interests are best served.

Those who rely on members expect them to discharge their responsibilities with integrity, objectivity, due professional care, and a genuine interest in serving the public. They are expected to provide quality services, enter into fee arrangements, and offer a range of services—all in a manner that demonstrates a level of professionalism consistent with these Principles of the Code of Professional Conduct.

All who accept membership in the American Institute of Certified Public Accountants commit themselves to honor the public trust. In return for the faith that the public reposes in them, members should seek to continually demonstrate their dedication to professional excellence.

Integrity

Integrity principle. To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity.

Integrity is an element of character fundamental to professional recognition. It is the quality from which the public trust derives and the benchmark against which a member must ultimately test all decisions.

Integrity requires a member to be, among other things, honest and candid within the constraints of client confidentiality. Service and the public trust should not be subordinated to personal gain and advantage. Integrity can accommodate the inadvertent error and honest difference of opinion; it cannot accommodate deceit or subordination of principle.

Integrity is measured in terms of what is right and just. In the absence of specific rules, standards, or guidance or in the face of conflicting opinions, a member should test decisions and deeds by asking: "Am I doing what a person of integrity would do? Have I retained my integrity?" Integrity requires a member to observe both the form and the spirit of technical and ethical standards; circumvention of those standards constitutes subordination of judgment.

Integrity also requires a member to observe the principles of objectivity and independence and of due care.

Objectivity and Independence

Objectivity and independence principle. A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities. A member in public

practice should be independent in fact and appearance when providing auditing and other attestation services.

Objectivity is a state of mind, a quality that lends value to a member's services. It is a distinguishing feature of the profession. The principle of objectivity imposes the obligation to be impartial, intellectually honest, and free of conflicts of interest. Independence precludes relationships that may appear to impair a member's objectivity in rendering attestation services.

Members often serve multiple interests in many different capacities and must demonstrate their objectivity in varying circumstances. Members in public practice render attest, tax, and management advisory services. Other members prepare financial statements in the employment of others, perform internal auditing services, and serve in financial and management capacities in industry, education, and government. They also educate and train those who aspire to admission into the profession. Regardless of service or capacity, members should protect the integrity of their work, maintain objectivity, and avoid any subordination of their judgment.

For a member in public practice, the maintenance of objectivity and independence requires a continuing assessment of client relationships and public responsibility. Such a member who provides auditing and other attestation services should be independent in fact and appearance. In providing all other services, a member should maintain objectivity and avoid conflicts of interest.

Although members not in public practice cannot maintain the appearance of independence, they nevertheless have the responsibility to maintain objectivity in rendering professional services. Members employed by others to prepare financial statements or to perform auditing, tax, or consulting services are charged with the same responsibility for objectivity as members in public practice and must be scrupulous in their application of generally accepted accounting principles and candid in all their dealings with members in public practice.

Due Care

Due care principle. A member should observe the profession's technical and ethical standards, strive continually to improve competence and the quality of services, and discharge professional responsibility to the best of the member's ability.

The quest for excellence is the essence of due care. Due care requires a member to discharge professional responsibilities with competence and diligence. It imposes the obligation to perform professional services to the best of a member's ability, with concern for the best interest of those for whom the services are performed, and consistent with the profession's responsibility to the public.

Competence is derived from a synthesis of education and experience. It begins with a mastery of the common body of knowledge required for designation as a certified public accountant. The maintenance of competence requires a commitment to learning and professional improvement that must continue throughout a member's professional life. It is a member's individual responsibility. In all engagements and in all responsibilities, each member should undertake to achieve a level of competence that will assure that the quality of the member's services meets the high level of professionalism required by these Principles.

Competence represents the attainment and maintenance of a level of understanding and knowledge that enables a member to render services with facility and acumen. It also establishes the limitations of a member's capabilities by dictating that consultation or referral may be required when a professional engagement exceeds the personal competence of a member or a member's firm. Each member is responsible for assessing his or her own

competence of evaluating whether education, experience, and judgment are adequate for the responsibility to be assumed.

Members should be diligent in discharging responsibilities to clients, employers, and the public. Diligence imposes the responsibility to render services promptly and carefully, to be thorough, and to observe applicable technical and ethical standards.

Due care requires a member to plan and supervise adequately any professional activity for which he or she is responsible.

Tools Available for Discipline

The SEC may bar or suspend from practice any accountant deemed to have engaged in “unethical or improper professional conduct.”⁸³ The state from which the accountant received his or her license can fine, suspend, or bar the accountant from practice. The Professional Ethics Division within the AICPA can initiate investigations into allegations of unethical or wrongful conduct if the CPA is a member of the AICPA. If it determines guilt, it can bar the accountant from AICPA membership. The auditing profession is subject to oversight by the PCAOB, and auditors remain subject to disciplinary actions by the PCAOB to ensure that they maintain compliance with auditing standards.⁸⁴

Author Information

Raj Gnanarajah
Analyst in Financial Economics

Acknowledgments

Marc Labonte and Eva Su provided comments. Amber Wilhelm assisted with graphics.

Disclaimer

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⁸³ 17 C.F.R. §201.

⁸⁴ PCAOB, “Enforcement,” <https://pcaobus.org/oversight/enforcement>.