

facilitate effective enforcement of the securities laws and criminal laws,<sup>38</sup> which requires the retention of not only records that *support* the auditor's report (as required by SAS 96) but also records that would be inconsistent with, or otherwise challenge, the conclusions in the auditor's report. In order to ensure that the purposes of the Act are fulfilled, we proposed that paragraph (c) of the rule include the specific requirement that the materials retained under paragraph (a) would include not only those that support an auditor's conclusions about the financial statements but also those materials that may "cast doubt" on those conclusions.<sup>39</sup> We stated in the Proposing Release that paragraph (c) was intended to ensure the preservation of those records that reflect differing professional judgments and views (both within the accounting firm and between the firm and the issuer) and how those differences were resolved. To better communicate what we intended by "cast doubt" on the auditor's conclusions, we included in the proposed rule the example of documentation of differences of opinion concerning accounting and auditing issues.

The auditor in a variety of contexts may create materials related to differences of opinion. For example, SAS No. 22, "Planning and Supervision," states in part:

The auditor with final responsibility for the audit and assistants should be aware of the procedures to be followed when differences of opinion concerning accounting and auditing issues exist among firm personnel involved in the audit. Such procedures should enable an assistant to document his disagreement with the conclusions reached if, after appropriate consultation, he believes it necessary to disassociate himself from the resolution of the matter. In this situation, the basis for the final resolution should also be documented.<sup>40</sup>

<sup>38</sup> See Statement of Senator Leahy on the Senate floor, 148 Cong. Rec. S7419 (July 26, 2002).

<sup>39</sup> Senator Leahy stated on the Senate floor:

In light of the apparent massive document destruction by Andersen, and the company's apparently misleading document retention policy, even in light of its prior SEC violations, it is intended that the SEC promulgate rules and regulations that require the retention of such substantive material, including material that casts doubt on the views expressed in the audit or review, for such a period as is reasonable and necessary for effective enforcement of the securities laws and the criminal laws, most of which have a five-year statute of limitations.

148 Cong. Rec. S7419 (July 26, 2002).

<sup>40</sup> SAS 22, ¶ 22 (as amended by SAS 47, 48 and 77); AU § 311.22. "Assistants," in the context of the first sentence of the quoted paragraph, is intended to include other partners who are on the audit engagement team.

An interpretation of this section issued by the AICPA's Auditing Standards Board emphasizes the professional obligation on each person involved in an audit engagement to bring his or her concerns to the attention of others in the firm and, as appropriate, to document those concerns. This interpretation states:

Accordingly, each assistant has a professional responsibility to bring to the attention of appropriate individuals in the firm, disagreements or concerns the assistant might have with respect to accounting and auditing issues that he believes are of significance to the financial statements or auditor's report, however those disagreements or concerns may have arisen. In addition, each assistant should have a right to document his disagreement if he believes it is necessary to disassociate himself from the resolution of the matter.<sup>41</sup>

In addition, SAS 96 states that the documentation for an audit should include the findings or issues that in the auditor's judgment are significant, the actions taken to address them (including any additional evidence obtained), and the basis for the final conclusions reached.<sup>42</sup> For example, if a memorandum is prepared by a member of a large accounting firm's national office that is critical of the accounting used by an audit client, or of a position taken by the partner in charge of the audit of those financial statements, that memorandum should be retained.<sup>43</sup> Another example would be documentation related to an auditor's communications with an issuer's audit committee about alternative disclosures and accounting methods used by the issuer that are not the disclosures or accounting preferred by the auditor.<sup>44</sup>

<sup>41</sup> "Planning and Supervision: Auditing Interpretations of Section 311," AU § 9311.37. "Assistants," in the context of this interpretation, includes other partners who are on the audit engagement team.

<sup>42</sup> SAS 96, ¶ 9; AU § 339.09, which states:

In addition, the auditor should document findings or issues that in his or her judgment are significant, actions taken to address them (including any additional evidence obtained), and the basis for the final conclusions reached.

See also, SAS 96, ¶ 6; AU § 339.06, which states:

Audit documentation should be sufficient to (a) Enable members of the engagement team with supervision and review responsibilities to understand the nature, timing, extent, and results of auditing procedures performed, and the evidence obtained; (b) indicate the engagement team member(s) who performed and reviewed the work; and (c) show that the accounting records agree or reconcile with the financial statements or other information being reported on.

<sup>43</sup> Such a memorandum might be prepared in connection with the consultation process that is part of an accounting firm's quality controls. See, e.g., section 103(a)(2)(B)(ii) of the Sarbanes-Oxley Act.

<sup>44</sup> Section 204 of the Sarbanes-Oxley Act adds section 10A(k) to the Exchange Act and requires

We continue to believe that retaining any materials that might cast doubt on the final conclusions reflected in the auditor's report, including those created under SAS 22 and SAS 96, would be consistent with the letter and spirit of the Sarbanes-Oxley Act. One commenter, the National Association of State Boards of Accountancy ("NASBA"), endorsed requiring the retention of documents that "cast doubt" on an auditor's audit or review because "state attorneys' general staff members assigned to accountancy boards often have complained of receiving only those documents that support the final report." NASBA also noted, however, that the Commission promptly should revise the rule if it becomes too burdensome or otherwise unworkable.<sup>45</sup>

Several commentators stated that the proposed "cast doubt" language was unworkable. They indicated that the phrase was pejorative,<sup>46</sup> vague and unnecessary, and might be used to attribute doubt to virtually any remark made during an audit, regardless of its relevance or materiality.<sup>47</sup> One accounting firm stated that the proposed rule "could be read to require retention of every document reflecting an error however temporary—even typographical or addition errors made in preparing a workpaper. \* \* \* It also could be read to require preservation of each and every exchange of differing views on any topic, however fleeting and trivial the differences."<sup>48</sup> Another accounting firm stated that on many occasions correcting or redoing workpapers is not the result of differences of opinion but from on-the-job training and a normal learning

auditors to report certain matters to audit committees, including: "(a) All critical accounting policies and practices to be used, (2) all alternative treatments of financial information within generally accepted accounting principles that have been discussed with management officials of the issuer, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the registered public accounting firm; and (3) other material written communications between the registered public accounting firm and the management of the issuer, such as the management letter or schedule of unadjusted differences."

<sup>45</sup> Letter from K. Michael Conaway, Chair, NASBA, and David A. Costello, President and CEO, NASBA, dated December 23, 2002.

<sup>46</sup> Letter from Donald G. DeBuck, Computer Sciences Corporation, dated December 26, 2002.

<sup>47</sup> See, e.g., letter from BDO Seidman, LLP, dated December 27, 2002; letter from Grant Thornton LLP dated December 27, 2002; letter from KPMG LLP dated December 27, 2002; letter from Deloitte & Touche LLP dated December 27, 2002.

<sup>48</sup> Letter from Ernst & Young LLP, dated December 27, 2002.