

investment companies filing financial statements with the Commission.<sup>68</sup> Each firm currently is required to perform its audits and reviews in accordance with generally accepted auditing standards ("GAAS"), which require auditors to retain certain documentation of their work.<sup>69</sup> Accounting firms, therefore, currently make decisions about the retention of each record created during the audit or review. GAAS, however, currently does not require explicitly that auditors retain documents that do not support their opinions and GAAS does not set definite retention periods. As a result, rule 2-06 might result in the retention of more records than currently required under GAAS, and might result in some accounting firms keeping those records for a longer period of time.

To cover all increases in burden hours, we estimated in the proposing release that, on average, the incremental burden on firms would be no more than one hour for each public company audit client, or approximately 15,000 hours.<sup>70</sup>

We received comments on the proposed collection of information requirements indicating that, in view of the possible breadth of the proposed rule, the estimated burden hours appeared to be low.<sup>71</sup> These commenters suggested that this burden would be mitigated by revising the portion of the proposed rule related to the retention of records that "cast doubt" on the final conclusions reached by the auditor on the audit or review.<sup>72</sup> In view of the revisions made to the rule and the clarifications in this release

provided in response to commenters' concerns, we believe that the estimated burden is reasonable.

#### IV. Cost—Benefit Analysis

The record retention requirements in rule 2-06 implement a congressional mandate. We recognize that any implementation of the Sarbanes-Oxley Act likely will result in costs as well as benefits and will have an effect on the economy. We are sensitive to the costs and benefits imposed by our rules and, in the Proposing Release, we identified certain costs and benefits of the proposed rule.

##### A. Background

Under section 802 of the Sarbanes-Oxley Act, accountants who audit or review an issuer's financial statements must retain certain records relevant to that audit or review. Rule 2-06 implements this provision and indicates the records to be retained, but it does not require accounting firms to create any new records.

The records to be retained would include those relevant to the audit or review, including workpapers and other documents that form the basis of the audit or review and memoranda, correspondence, communications, other documents, and records (including electronic records), which are created, sent or received in connection with the audit or review, and contain conclusions, opinions, analyses, or financial data related to the audit or review. Records described in the rule would be retained whether the conclusions, opinions, analyses, or financial data in the records support the final conclusions reached by the auditor, or contain information or data, relating to a significant matter, that is inconsistent with the final conclusions of the auditor on that matter or the audit or review. The required retention of audit and review records should discourage the destruction, and assist in the availability, of records that may be relevant to investigations conducted under the securities laws, Commission rules or criminal laws.

##### B. Potential Benefits of the Retention Requirements

Rule 2-06 requires that accountants retain certain records relevant to an audit or review of an issuer's or registered investment company's financial statements for seven years. To the extent that the rule increases the availability of documents beyond current professional practices, the rule may benefit investigations and litigation conducted by the Commission and others. Increased retention of these

records will preserve evidence reflecting significant accounting judgments and may provide important evidence of financial reporting improprieties or deficiencies in the audit process.

One of the most important factors in the successful operation of our securities markets is the trust that investors have in the reliability of the information used to make voting and investment decisions. In addition to providing materials for investigations, the availability of the documents subject to rule 2-06 might facilitate greater oversight of audits and improved audit quality, which, in turn, ultimately could increase investor confidence in the reliability of reported financial information.

##### C. Potential Costs of the Proposal

In the proposing release, we estimated that approximately 850 accounting firms audit and review the financial statements of approximately 20,000 public companies and registered investment companies filing financial statements with the Commission.<sup>73</sup> Each firm currently is required to perform its audits and reviews in accordance with generally accepted auditing standards ("GAAS"), which require auditors to retain certain documentation of their work.<sup>74</sup> Accounting firms, therefore, currently make decisions about the retention of each record created during the audit or review. GAAS explicitly requires that auditors retain documents that support their audit reports, but it does not set definite retention periods. As noted above, to ensure the purposes of the Act are achieved, the final rule requires the retention of materials that not only support the auditor's report but also records that are inconsistent with that report, and sets a seven-year retention period. As a result, rule 2-06 might result in the retention of more records than currently required under GAAS, and might result in some accounting firms keeping those records for a longer period of time.

It is important to note, however, that the proposed rules do not require the creation of any record; they require only that existing records be maintained for the prescribed time period. It also is important to note that decisions about

<sup>68</sup> These estimates are based on information in Commission databases. The number of public companies includes those filing annual reports and those filing registration statements to conduct initial public offerings. The same auditors also audit the financial statements of approximately 5,587 investment companies.

<sup>69</sup> See American Institute of Certified Public Accountants ("AICPA"), Statement on Auditing Standards No. ("SAS") 96, "Audit Documentation"; Codification of Statements on Auditing Standards ("AU") 339. GAAS does not specify a required retention period. The documents to be retained under SAS 96 include those indicating the auditing procedures applied, the evidence obtained during the audit, and the conclusions reached by the auditor in the engagement.

<sup>70</sup> This burden accounts for incidental reading and implementation of the rule. Fifteen thousand burden hours should be sufficient to cover the audits and reviews of not only public companies but also registered investment companies. Because of the nature and scope of the audits of investment companies, there would be an even smaller and insignificant incremental burden imposed on those audits than on the audits of public companies.

<sup>71</sup> See letter from Lynette Downing, HLB Tautges Redpath, Ltd. dated December 27, 2002; letter from PricewaterhouseCoopers dated December 27, 2002; letter from Deloitte & Touche dated December 27, 2002.

<sup>72</sup> See letter from PricewaterhouseCoopers dated December 27, 2002 and letter from Deloitte & Touche dated December 27, 2002.

<sup>73</sup> These estimates are based on information in Commission databases. The number of public companies includes those filing annual reports and those filing to conduct an initial public offering. The same auditors also audit the financial statements of approximately 5,587 investment companies.

<sup>74</sup> See American Institute of Certified Public Accountants ("AICPA"), Statement on Auditing Standards No. ("SAS") 96, "Audit Documentation"; Codification of Statements on Auditing Standards ("AU") 339.