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C O N T E N T S

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Opening Remarks - Chairman Christopher Cox

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Mark Olson, Chairman

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Public Company Accounting Oversight Board

Jeff Steinhoff, Managing Director,

Financial Management and Assurance

US Government Accountability Office

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Conrad Hewitt, Chief Accountant

Office of the Chief Accountant

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John White, Director

Division of Corporation Finance

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Zoe-Vonna Palmrose, Deputy Chief Accountant

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1           Over the past several years, the GAO has undertaken  
2 extensive work in studying the implementation of the  
3 Sarbanes-Oxley Act. This work includes at least nine studies  
4 and analyses of various aspects of Sarbanes-Oxley  
5 implementation and it is focused in particular on the special  
6 challenges of applying the Section 404 requirements to  
7 smaller public companies.

8           Thus far, smaller public companies have not had to  
9 comply with Section 404. But beginning next year, smaller  
10 companies will be expected to come into compliance, and so it  
11 is vitally important that we have a scalable approach that  
12 works for them. Both the Commission and, as we've just heard,  
13 the PCAOB are focused on this and we have been urged by  
14 congressional leaders including House Financial  
15 Services Committee Chairman Barney Frank,  
16 Senate Small Business Committee Chairman John  
17 Kerry, and House Small Business Committee Chair,  
18 Nydia Velazquez -- to ensure that the Section 404  
19 process is scalable for small businesses. And because these  
20 committees have cited to us the importance of GAO's report on  
21 the implementation of Section 404 for smaller companies, I am  
22 especially pleased that Mr. Steinhoff can be here with us  
23 today. We look forward to hearing from you about the GAO's  
24 views on the implementation of Sarbanes-Oxley Act for smaller  
25 public companies.





















































1                   What we are really trying to do is make this a more  
2 effective audit process thinking in terms of an integrated  
3 audit which I think is an important element for both large  
4 and small companies alike. We never think in terms of  
5 efficiency without thinking about what is the impact on audit  
6 effectiveness. And, if it's positive, that's great. If it's  
7 neutral, okay. But there is never any thought about  
8 compromising audit effectiveness to obtain so-called  
9 efficiencies.

10                   In other words, efficiency is about unnecessary  
11 work that actually can diminish audit quality, not improve  
12 it.

13                   CONRAD HEWITT: I would like a footnote. As  
14 Zoe-Vonna has just said about the investor, protection of the  
15 investor, that excessive cost of an audit harms the investor's  
16 value in that company in the marketplace. Those costs can be  
17 used for other more important things of the company, such as  
18 customer satisfaction, product development and those types of  
19 things. So there has to be a good balance and that's what  
20 we're trying to approach here is a good balance for the  
21 investor.

22                   COMMISSIONER CAMPOS: I trust no one at any policy  
23 level has indicated to you that investor interests and  
24 investor protection is less important?

25                   MS. PALMROSE: No, not at all. In fact, that's what

1 we are constantly thinking about. And, as I said just to  
2 reinforce, we believe, we firmly believe that investors in  
3 all companies are entitled to these disclosures and that this  
4 is doable and that's what we are working to achieve.

5 COMMISSIONER CAMPOS: I think Mike Gaynor put it to  
6 me another way when we were -- when he was briefing  
7 me, and he said that the goal of this process, I  
8 quote, "is to increase both the effectiveness of the audit  
9 and the efficiency in conducting the audit and if the only  
10 outcome of a proposed change to the standard is fewer  
11 disclosures to investors and less public reporting without  
12 gains in both the effectiveness and efficiency, then there is  
13 no reason to make a change."

14 Is that a fair summarization of what we're trying  
15 to do?

16 MS. PALMROSE: Well, let me speak for my staff.  
17 Oftentimes Mike is very eloquent. He also has a great wit,  
18 too.

19 COMMISSIONER CAMPOS: I thought he was witty, too.

20 MS. PALMROSE: I can't dispute that. But the answer  
21 is it's very well stated.

22 COMMISSIONER CAMPOS: I'm trying to fit my sub-  
23 questions where I can still say it's only been two questions.

24 MS. PALMROSE: We're auditors here.

25 COMMISSIONER CAMPOS: But are you using judgment?

































1 CHAIRMAN COX: Zoe-Vonna?

2 MS. PALMROSE: I was just going to add we did that  
3 in Management Guidance and got positive feedback on that. So  
4 we thought it might be a useful approach within the auditing  
5 standard, too.

6 CHAIRMAN COX: This leads us into another topic.

7 Nancy, you mentioned extending this throughout the  
8 standard. What does the SEC staff mean when we talking about  
9 extending the scaling concept throughout the PCAOB standard?  
10 What exactly does that mean?

11 MS. SALISBURY: Well, as Zoe-Vonna mentioned, in the  
12 Management Guidance, we tried to provide in places where we  
13 thought it was appropriate and beneficial, we tried to  
14 provide illustrative examples for specifically what smaller  
15 companies could anticipate or potentially how a smaller  
16 company approach might be different and we thought that it  
17 would be helpful if the PCAOB challenged their standard and  
18 looked for situations or areas where they could do the same  
19 to better illustrate the principles in the scaling section.

20 CHAIRMAN COX: So the approach to extension is  
21 illustration and we would sprinkle those throughout the  
22 standard?

23 MS. PALMROSE: Illustration is probably -- your  
24 vocabulary is so wonderful, you would probably get a little  
25 more precise term here --



















































































1                   So we appreciate it, but we also appreciate the  
2           importance of internal controls for interim and annual  
3           financial reporting. And we have no conclusion on this.  
4           It is just an area that we have received comment on.  
5           The PCAOB solicited comment on it, got a number of comments  
6           and we will be talking about it.

7

8                   COMMISSIONER CASEY: Thank you.

9                   CHAIRMAN COX: Is there any further discussion on  
10          this point?

11                   (No response.)

12                   CHAIRMAN COX: If not, I will summarize the staff's  
13          recommendation on use of judgment and ask the Commissioners  
14          to express support or disagreement with this approach.

15                   Specifically on the use of judgment and testing and  
16          evaluation, the SEC staff proposes to work with the PCAOB  
17          staff, first, to ensure that the auditor has the latitude to  
18          establish the level of evidence required based upon the  
19          auditor's assessment of risk.

20                   Second, to ensure that the auditor can make  
21          appropriate use of management's risk assessment and  
22          monitoring activities in determining the audit procedures.

23                   And, third, to explore the relationship between the  
24          auditor's communications of significant deficiencies and  
25          management's responsibilities in this area.











































