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United States Senate
WASHINGTON, DC 20510

January 17, 2007

The Honorable Mark W. Olson
Chairman
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, D.C. 20006-2803

Dear Chairman Olson:

After the passage of the Sarbanes-Oxley Act (the "Act"), the American public has seen the enormous benefits achieved by renewed confidence in our markets. However, these benefits have carried a high price, and many companies have struggled to implement the provisions of the Act, especially Section 404. I have been vocal in the need for company and auditor guidance to help smooth the implementation of Section 404 and reduce costs. I am pleased that the Securities and Exchange Commission (the "SEC") and the Public Company Accounting Oversight Board (the "Board") listened when, late last year, they issued cooperative guidance to help lower the costs of the Act for public companies, especially small public companies.

The SEC and the Board face the tough challenge of balancing efficiency and reliability in company audits. In an effort to find this balance, I am pleased that the Board has decided to take another look at their auditor guidance to find new ways to reduce costs for large and small businesses. I have included more detailed comments on the Board's proposal below.

One of the most important revisions made by the Board, and one of the biggest potential cost-savers, is in the auditor's use of the work of others. This includes company management's own internal control evaluation, as well as past audits. Duplicating control evaluations despite low relative risk multiplies audit costs unnecessarily. Allowing auditors to evaluate and utilize past work would allow them to focus resources on high-risk areas and reduce costs.

One of the biggest ways the Board is promoting this new auditor culture is by removing the "Principle Evidence Provision" from the standard. This will encourage a more cumulative understanding of a company's financial health, as well as help integrate the financial statement audit and the internal control audit.

From an auditor's standpoint, a clear understanding of risk and the severity of a control deficiency is crucial to implementing a top-down audit approach. The Board is encouraging efficiency by clarifying and refining the definition of "material weakness" and "significant deficiency", as they do in Appendix 1, paragraphs 70-79 of the new standard. I have heard several examples of audit costs skyrocketing when auditors are unsure about material weaknesses and abandon a risk-based assessment to chase down problems that are neither significant nor material. These cases can be avoided when auditors are confident in their ability to target the most significant control deficiencies in a company.

The Board correctly recognizes that their changes to Auditing Standard No. 2 hold the most potential benefit for small companies. Since the drafting stages of the Sarbanes-Oxley Act, I have been concerned with the disproportionate impact the law would have on smaller public companies, and those attempting to access the public markets for the first time. In a Government Accountability Office (GAO) report requested by myself and Chairwoman Snowe, these concerns were proved to be well-founded. According to that report, small companies who had implemented section 404 in 2004 paid a median amount of $1.14 in audit fees for every $100 in revenues, compared to only $0.13 per $100 for larger companies. While some of this money was dedicated to the financial statement audit, the internal control audit undoubtedly consumed a large portion of this cost. There is a connection between the size of a company and the functioning of their internal controls and, as shown by this GAO report, small business auditors have not been quick to recognize these differences and modify the scope of their audits accordingly.

Despite these statistics, I am confident that small company audits will become more efficient than in the past due to the Board's emphasis on scalability for small companies. For example, the segregation of duties at a company with 10 employees is necessarily different than those of a 1,000 employee company. Management may be intimately involved in the day-to-day operations of a small company, yet past audits did not reflect that difference. It is crucial that auditors now recognize the unique operations of small business and adapt audits accordingly. It is the Board's responsibility to actively promote this change, even after the new guidance is adopted, to ensure that audit costs do not become prohibitively high for small business.

On a related note, I am pleased that the Board has decided to continue holding their Forums on Auditing in the Small Business Environment. The Board has an exemplary record of reaching out to the accounting community. These forums have helped accountants prepare for internal control audits as well as provided crucial input to the Board on their guidance. As most small business have yet to experience a Section 404 audit, the need for capable small business auditors will only increase as implementation continues.

I am hopeful that the Board's revisions to Auditing Standard No. 2 will significantly reduce costs for public companies, especially smaller public companies with limited resources and those preparing to go public. This is an evolving process, and full implementation has not yet been achieved. But the Sarbanes-Oxley Act has been crucial in protecting the confidence of our public markets, and I am dedicated to ensuring that the American markets remain the gold standard for the world.

Sincerely,

Michael B. Enzi

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U.S. Senator