Opening remarks of H. Stephen Meisel,
Partner, PricewaterhouseCoopers, speaking on behalf of the Center for Audit Quality
before the SEC's Advisory Committee on Improvements to Financial Reporting

March 13, 2008

Chairman Pozen and members of the Committee, SEC staff and observers, good afternoon. Thank you for inviting me here today to respond to your questions on behalf of the Center for Audit Quality relating to the developed proposals for materiality assessments and the process for reporting errors.

Although the number of restatements declined in 2007, the number of restatements has grown substantially over the last several years. The Committee's Progress Report describes a number of contributing factors for this growth, including an observation that it may be a result of an overly broad application of existing materiality guidance. The terms 'unnecessary' and 'necessary' have been used when describing restatements creating a perception that some restatements are being processed for immaterial items – items that are not important to a reasonable investor. This leads us to question whether the errors that were determined to be material were, in fact, not material and whether the disclosures of the error correction were useful to investors. To provide better information to the market, additional guidance on materiality judgments and, separately, the process for and disclosure of the correction of errors should be enhanced.

The three key themes to materiality and error correction guidance are:

1. All errors need to be corrected, yet not all need to result in a restatement;
2. The materiality of an error should be evaluated from the perspective of a reasonable investor and should consider all surrounding facts and circumstances; and
3. Transparent disclosures are essential to communicating material errors to investors.

The Committee's recommended enhancements to existing SEC materiality guidance should not be viewed as facilitating the obfuscation of material errors or permitting material errors to remain uncorrected under the guise of qualitative judgments. In fact, all errors need to be corrected so that a company's underlying financial records are complete. It is determining what constitutes a material error and how the error should be corrected and disclosed that warrants enhancement.

It is important to align materiality judgments with investor needs. The materiality of any one piece of information should be judged based on the total mix of information. For example, an interim period is part of a larger mix of information available to a reasonable investor. That is not to suggest that interim financial statements are unimportant. Rather, it is an acknowledgement that certain factors are evaluated differently in the materiality analysis relating to interim financial statements. As such, there may be instances when an amount that might appear to be large would be unimportant to a reasonable investor when viewed within the context of all of the surrounding facts and circumstances. Likewise, there may be instances when an amount that might appear to be small would be important to a reasonable investor given the surrounding facts and circumstances.

Transparent disclosures should be provided to inform investors:

- That a material error occurred;
- The impact of the error on the period in which it originated and the period in which it is corrected; and
- Any implications the error has on the company's business.

These disclosures should provide comparable financial data and insight regarding the likelihood that such an error could occur in the future.

In summary, there are two separate and distinct steps. First, the determination of whether or not an error is important to an investor given all the surrounding facts and circumstances. Second, the forms of disclosure for the correction of an error that is important to a reasonable investor, such as restate prior periods or correct in the current period. The Committee's recommendations will enhance the usefulness of information provided to investors regarding the correction of errors in financial reporting.

Again, thank you for giving me the opportunity to share these perspectives with you; I would be pleased to respond to your questions and comments to assist the Committee in this important matter.