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CardinalHealth

November 14, 2003

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D. C. 20006-2803

Dear Board Members:

Cardinal Health, Inc. ("Cardinal") respectfully responds to the invitation to comment on *Proposed Auditing Standard-An Audit of Internal Control Over Financial Reporting Performed in Conjunction With an Audit of Financial Statements* ("Document"). Cardinal is a leading provider of products and services supporting the health-care industry. Cardinal, which is headquartered in Dublin, Ohio, employs more than 50,000 people on five continents and produces annual revenues of more than $50 billion. We appreciate this opportunity to provide you with our views on the Document.

As Cardinal is not a public accounting firm, a number of questions were not applicable or it was not appropriate for Cardinal to respond. As such, Cardinal's responses to select questions are listed below. The question from the Document is restated in bold type and Cardinal's response follows in normal type.

- **Question 1: "Is it appropriate to refer to the auditor's attestation of management's assessment of the effectiveness of internal control over financial reporting as an audit of internal control over financial reporting?"**

  No, we do not believe that it is appropriate to refer to the work proscribed by the relevant provisions of the Sarbanes-Oxley Act ("Act") as an audit because it is our belief that in order to do such the rules are inaccurately interpreting the mandate of the Act. The Act specifically calls for an attestation of management's assertion, not for an audit of the internal control structure. We believe that the PCAOB rules should only address what Congress mandated in the Act and not expand upon them.

- **Question 8: "Is it appropriate to state that inadequate documentation is an internal control deficiency, the severity of which the auditor should evaluate? Or should inadequate documentation automatically rise to the level of significant deficiency or material weakness in internal control?"**

  We believe that it is appropriate to state that inadequate documentation is an internal control deficiency, the severity of which should be evaluated by the auditor. However, the rules should not lose sight of the fact that the key objective is to provide investors with assurance that the company has an effective system of internal controls surrounding financial reporting in place and operating. Lack of adequate documentation may in fact be just that, while strong controls are in place and operating effectively.

- **Question 13 and Question 14: "Are the three categories of controls and the extent to which the auditor may rely on the work of others appropriately defined?" and "Does the proposed standard give appropriate recognition to the work of internal auditors? If not, does the proposed standard place too much emphasis and preference on the work of internal auditors or not enough?"**

  Regarding paragraph 104, we strongly disagree with prohibiting the use of the results of testing performed by a competent and objective internal audit function in the following areas:

  - Controls over the period-end financial reporting process, and
  - Information technology general controls on which the operating effectiveness of other controls depend.

  Internal audit functions routinely exhibit complete competence in performing this work and are, in most cases, not involved in the design and performance of procedures in both of these areas. To completely discount and disregard the validity of past reliance that the independent auditors have placed on internal auditors in financial statement audits is in no way justified. We would concur that the independent auditor should exercise careful judgment in these areas as to how much re-performance of the internal auditor's work should occur, but to dismiss the value that a competent and objective internal audit function can contribute in these areas is ungrounded, especially internal audit functions that are complying with professional standards established by the Institute of Internal Audit's "Standards for the Professional Practice of Internal Auditing."

  Similarly, the guidance in paragraph 10 that the use of procedures performed by internal audit should be limited for non-routine and nonsystematic transactions plus areas where the risk of control failure is high seems unduly restrictive. It would, perhaps, be more reasonable for the standard to require the independent auditor obtain direct independent evidence in these areas to complement the work done by the internal auditor. However, to proscribe that in all cases the independent auditor's use of internal audit's work in these areas be limited is an unmerited diminution of the effectiveness and reliability of a competent internal audit function.

- **Question 17: "Will the definitions in the proposed standard of significant deficiency and material weakness provide for increased consistency in the evaluation of deficiencies?"**

  While the new definitions may promote consistency, we believe that the new definitions are too restrictive and may be interpreted as setting unrealistically low thresholds. We believe that the concept of "remote likelihood" and "more than inconsequential" used to define a significant deficiency and "remote likelihood" used to define a material weakness set unnecessarily low hurdles for companies. We believe that lowering the threshold will have unintended and chilling consequences in the business world and urge the PCAOB to reconsider these definitions before issuing the final rules. In addition, we would like to see the final rules address the role of mitigating controls in the text and examples. Finally, we believe that further clarity is required affirming that a significant deficiency or material weakness is not automatically present in financial processes involving a large volume of transactions that requires reserve provisions for transactional conflicts pending further research and negotiation. We believe these situations would typically not be considered as a significant deficiency or material weakness.

- **Questions 25 and 26: "Is it appropriate that the existence of a material weakness would require the auditor to express an adverse conclusion about the effectiveness of the company's internal**

control over financial reporting, consistent with the required reporting model for management?" and "Are there circumstances where a qualified "except for" conclusion would be appropriate?"

Paragraph 115 of the draft standard essentially states that if the independent auditor determines that there is a material weakness, then an adverse report must be issued. This requirement, when taken in combination with the new material weakness definition in paragraph 9 imposes a substantially lower hurdle that in our view is unrealistic. "Remote likelihood" appears to be an unnecessarily conservative and somewhat arbitrary restriction for a judgment that will result in an adverse report. In addition to reconsideration of "remote likelihood," we believe there should be some reconsideration of a qualified report for isolated or less pervasive material weakness situations, reserving the adverse report for those circumstances with several material weaknesses and an overall weak control environment.

- **Other matters:**
  - Cardinal is a company that will, under current regulations, be required to provide management certification and auditor attestation in its annual report for the year ended June 30, 2004. As such we are currently working to meet these anticipated requirements. This process is a significant undertaking and, given the fact that the PCAOB will not even propose final rules to the SEC until January 2004 and that the SEC will not issue final rules until sometime thereafter, it seems unrealistic to hold companies to an effective date of 6/15/2004. We urge the PCAOB to request the SEC to delay the effective date until a later date, to ensure the appropriate amount of time to get this critical auditing standard right the first time.
  - We urge the PCAOB to provide guidance or relief in situations where major acquisitions occur close to a company's fiscal year end. The proposed rules should not hinder how businesses operate but the magnitude of work involved to evaluate acquired companies financial reporting internal control structures will hinder management's ability to attest as of fiscal year end when large acquisitions have been completed in a close proximity to the acquirer's fiscal year end.

Sincerely,

Richard J. Miller

Richard J. Miller
Chief Financial Officer

CC: John Finn, Audit Committee Chairman