W. R. Grace & Co.
7500 Grace Drive
Columbia, MD 21044

T 410.531.4185
F 410.531.4226
E robert.tarola@grace.com
W grace.com

Robert M. Tarola
Senior Vice President and
Chief Financial Officer

February 26, 2007

Office of the Secretary
Public Company Accounting
Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 021
Proposed Changes to Auditing Standard No. 2

GRACE

I appreciate the opportunity to comment on the Board's proposed changes to AS2. Set forth below are my responses to each question with commentary, as necessary, to explain my perspective on the issue.

Question 1

No. Although directionally sound, the proposed standard does not provide sufficient guidance about risk factors that should be considered when planning an audit. A top-down approach should result in a more effective audit, but it needs to start at the "very top" and include factors that impact market valuations, company strategy and organizational risk. Guidance should be expanded to include obtaining an understanding of over-arching control characteristics and assessing audit implications in the following areas:

- Market value drivers and analyst expectations;
- Governance structure, particularly for non-US subsidiaries;
- Audit committee diligence and accounting expertise;
- HR and pay practices toward accounting/finance professionals;
- Competency of accounting/finance/legal professionals;
- Accounting literacy of executives and key process owners;
- The degree of centralized vs. decentralized control;
- The client's risk profile and appetite; and,
- The client's "real" ethical culture as reflected in actions.

I am advocating a more "enterprise risk" approach, which will require both better guidance and a new focus of training for most auditors. It will be critical for an auditor to have a working knowledge of corporate finance, industry/company value factors, and sound risk mitigation approaches to effectively determine how best to apply a top-down risk-based set of audit tests and procedures.

Question 2

Yes, but more and specific guidance should be considered regarding factors that may encourage fraud such as reward system biases and cultural impediments to bad news. Also, the Board should consider how best to link the CEO/CFO certifications (under SOX Section 302), regarding responsibility to prevent and detect fraud, with the work of external auditors. Auditors should be required to assess the processes used by certifying officers to make their fraud-related assertions, and conclude if such are effective in the auditors' report on controls.

Question 3

Yes, it should. Obtaining a working understanding about how client executives assess and address risk is key to an effective top-down audit.

Question 4

Yes, it seems to. However, it could be made clearer regarding how to assess and conclude that lower level work can, indeed, be eliminated.

Question 5

Yes.

Question 6

Yes.

Question 7

Yes, but. The determination of "important enough to merit attention" requires the auditor to have a relative sense of risk that may, more often than not, result in most deficiencies being judged significant.

Question 8

No. More guidance is needed to help auditors understand enterprise risks and direct them to evaluate such risks in the context of financial reporting. For example, HR practices and philosophy can encourage the attraction, retention and development of qualified finance professionals, or discourage the same.

Question 9

Yes, they should.

Question 10

These changes make sense. The problem is that auditors need guidance on how to view deficiencies from a top-down perspective. For instance, at what level in the financial reporting process should a problem be identified? Is it ok if the CFO or CEO find a problem? It may be that they are the only individuals that had all the facts and indicators to identify it. This area will likely continue to be misapplied in practice without better guidance.

Question 11

Should be enough.

Question 12

Yes, the reference should be removed. Materiality relative to control testing should be determined from a full year perspective only. Also, guidance is needed on making judgments of materiality especially when income is small relative to the size of the enterprise.

Question 13

Yes, it should. Good change!

Question 14

Yes, they should.

Question 15

Yes.

Question 16

Yes.

Question 17

In almost all circumstances. The current requirement for selective tests of details is not a productive way to assess controls.

Question 18

Yes, it should.

Questions 19-25

These changes appear reasonable and well designed. I caution, however, to require auditor diligence in assessing qualifications of others and not simply accept advertised credentials or expertise.

Question 26

Yes, it should.

Question 27

No. This change is not likely to lower cost, but it may lower quality. Suggest it not be implemented.

Questions 28-32

This guidance seems appropriate at this time.

Question 33

This process appears sufficient.

Question 34

Target an effective date by mid-year 2007.

****

I would be pleased to clarify or otherwise address of any of my responses as the Board or Staff may desire.

Sincerely,

Robert M. Tarola

Robert M. Tarola