MAZARS

London and Paris, February 26, 2007

Public Company Accounting Oversight Board
Office of the Secretary
1666 K Street, N.W.
Washington, D.C. 20006-2803
Attention: J. Gordon Seymour, Secretary, and Members of the Board

Re: PCAOB Rulemaking Docket Matter No. 021 – Release N° 2006-007 December 19, 2006 Proposed Auditing Standard – An audit of internal control over financial reporting that is integrated with an audit of financial statements and related other proposals

Dear Sirs,

Mazars, an international, integrated and independent organization, comprising in 2006 5,600 staff and partners working in 38 countries (and more than 7,000 employees in our worldwide integrated partnership in 40 countries as of January 1st, 2007), and with all its associated practices able to mobilize 13,000 professionals in 58 countries, hereby represented by Mazars LLP (United Kingdom firm in London) and Mazars & Guérard (French firm in Paris), is pleased to submit this letter in response to the request for comments from the Public Company Accounting Oversight Board (the "Board") on its Proposed Auditing Standard – An audit of internal control over financial reporting that is integrated with an audit of financial statements and related other proposals (together the "PCAOB AS No. 2"), in accordance with Section 404 and 103 of the Sarbanes-Oxley Act of 2002 (the "Act"). We appreciate the opportunity to comment on this PCAOB Release.

In North America, Mazars has a long standing presence via Mazars USA (created in 1988/1989, and registered with the PCAOB). As a natural extension of its development strategy, Mazars has formed several joint ventures with members of Moores Rowland International (MRI) since 2000 to assist its clients in various corners of the world. At the end of 2006, Mazars and the American members of MRI, decided to optimize their relationship. Mazars and Moores Rowland International have signed an agreement to launch a new international alliance between independent structures, named Praxity: its ambition is to allow each of these structures to offer national and international clients a service which conforms to the highest standards of professional excellence and ethics. Praxity, an international non-profit association registered in Belgium, will become operational in 2007.

We want to preface our specific comments with general consideration that we fully support implementation of rules strengthening the audit quality, and the contribution of these rules to restore the public confidence in financial reporting and in the world's capital markets. Mazars LLP and Mazars & Guérard are therefore fully committed to support PCAOB initiative, as well as those of IFAC, European Commission and other key European or national regulators that have been already doing good work and are implementing stronger controls in these areas of common concern.

We welcome the opportunity to comment the Proposed Auditing Standard on a subject we consider improving the audit quality. Please find hereafter our comments.

General comments

Item 2: Release of 2006-007

- Proposed Auditing Standard No. 2 discussion paper – Key thoughts
  1. The importance of risk assessments is highlighted. This should reduce the problems of over-auditing both geographically and in the number of controls to be considered 'key'. This will be easier for accelerated filers as the information upon which to base risk assessments should now be available and more robust. For non-accelerated filers we are concerned that they will not be aware of the increased planning that is required to achieve the eventual reduction in work. The guidance in RIN 3235-AJ58 will be useful but is perhaps more theoretical than practical in application.
  2. A large number of problems associated with implementing AS 2 in the past have been caused by the 'fear factor'. This is what some people in management of the companies complying with SOX call the attitude of the external auditors. The concern from people we have spoken to is that the guidance does not materially reduce the 'fear factor' and that until external auditors publicly state how they will be treated, they will assume nothing has changed from the previous AS 2.
  3. The guidance does allow for some proportionality of controls depending on the size and complexity of the business, and this is to be welcomed. It is, however, difficult to place reliance on key controls that are not capable of demonstration, especially when this is combined with a reduction in the controls that are considered to be 'key'. We are concerned that this, though good in theory, will prove difficult in practice.
  4. The new definitions for deficiency, significant deficiency and material weakness are welcomed as this should help to reduce the scope, which is at least in part the intention of the amendments.
  5. The use of prior results in considering the extent of testing is interesting. It is a little unclear in the guidance what effect previous testing has on a control and for how long reliance can be placed on it. Would, for example, a walkthrough determining that the control had not changed be sufficient or would testing need to be undertaken with a reduced sample size etc…? Although the standard should not aim to be prescriptive in all respects, more guidance in this area would be useful as it is already being debated by companies and, in our experience, also external auditors.
- Proposed amendments to the Boards interim standard
  1. No specific comments to make
- Proposed interpretive guidance
  1. The proposed guidance is an useful information, but more a theoretical guide than a practical one. For example, little or no mention is made of consultation with external auditors when implementing a risk based approach. In practice, consultation with external auditors in all scoping matters has led to a better SOX experience.

Item 3: Release of 2006-007

- Extension of implementation deadline for non-accelerated filers etc…

Under the amendments, management would be required to issue their Management Report on Internal Control for years ending on or after 15th December 2007 and auditor attestation for years ending on or after 15th December 2008. The SEC has indicated that it may consider further delay based on the implementation of the revised AS 2.

The reasons given by the PCAOB for the delay are persuasive. Developments since the last delay was issued include the finalization of guidance for small companies from COSO, the GAO principles paper, the advisory report on smaller companies to the commission, changes to AS 2 and a consultation of commentators on proposed extension dates.

However, we would caution the following:

- Work expands to fill the time available to perform it. We have seen this with the previous delays as companies begin to comply, stop, and then begin again. In addition, this demonstrably weakens the ability of the company to introduce good remediation practices and achieve management buy in for the process;
- While the reasons for the delay are good and should provide relief for companies that apply all the new guidance in an effective manner, we believe that consideration should be given to a positive statement that this is intended to be the last delay – We are very concerned that companies are now wallowing in inertia in the hope that further delays and legislative challenges will reduce further their compliance burden. The result of this is that they will not be ready for the introduction of the Act as little/no work is currently being undertaken to comply. This appears to contradict one of the goals of the Act by allowing management to postpone their responsibility of ensure that they have implemented an effective system of internal controls over financial reporting.

We agree with the decision not to increase the relief to companies that currently are non-accelerated filers but become accelerated filers before December 15, 2008. We believe that an extension of this rule would cause confusion both within the companies concerned and within the investor community.

We approve of the additional disclosure requirement requiring non-accelerated filers to state that their controls will not have been subject to auditor attestation. We see no reason to exclude FPI's from this additional requirement as it will ease transparency and uniformity.

We approve of the proposed transition period for newly public companies, assuming that the appropriate disclosure of this is made.

Detailed comments, with answers to the questions

1. Does the proposed standard clearly describe how to use a top-down approach to auditing internal control?
We consider that the description provided is helpful. However, it's not clear that once an account is identified as a significant account, if the auditor must then identify all assertions related to that account and test the related controls, or if they may test the control surrounding the assertion that is considered to present a reasonable possibility of material misstatements. Example, if accounts receivable net is identified as a significant account based on qualitative factors surrounding the allowance for doubtful accounts (the valuation assertion), must the auditor identify and test controls surrounding all assertions related to accounts receivable net or only those controls related to the provision for doubtful accounts?

2. Does the proposed standard place appropriate emphasis on the importance of identifying and testing controls designed to prevent or detect fraud?
We consider that emphasis is appropriate. However, this element deserves more guidance in order to better link what should be done for an integrated audit compared to what is usually done when auditing financial statements. Otherwise, this could lead to an expectation gap between work performed by auditor and expectation from users. Guidance could be provided in order to require the auditor:
- to evaluate the design of system of detection or prevention of fraud set up by the management,
- to require the auditor to perform walkthrough on key controls designed to detect or prevent fraud.
Testing operating effectiveness of fraud controls is difficult, but back to some basics should be reminded. It could be for example controls regarding segregation of duties, cash authorization.

Moreover, we suggest a modification in the auditor's report, given the inherent risk in internal controls due to management override:
"[Inherent limitations paragraph]
Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements **or fraud**. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate."

3. Will the top-down approach better focus the auditor's attention on the most important controls?
Generally yes, however clarification is needed regarding whether controls related to all assertions for each significant account identified require testing, or only those assertions considered to contain a reasonable possibility of material misstatement.

4. Does the proposed standard adequately articulate the appropriate consideration of company-level controls and their effect on the auditor's work, including adequate description of when the testing of other controls can be reduced or eliminated?
We believe that paragraphs 43 and 44 sufficiently address this issue. However, within these paragraphs, we believe that the references made to misstatements should be altered to made reference to "material" misstatements.
Regarding timing of testing in paragraph 17, it might be useful to note that a "test" of company level controls includes testing both the design and operation of the controls.

5. Does the proposed standard appropriately incorporate risk assessment, including in the description of the relationship between the level of risk and the necessary evidence?
We believe it provide adequate guidance.

6. Would the performance of a walkthrough be sufficient to test the design and operating effectiveness of some lower risk controls?
Yes; however in paragraph 52, one of the factors affecting the risk associated with a control is the nature and **materiality** of the misstatement that the control is intended to prevent or detect. If there is the presumption that a correctly executed top-down approach would lead the auditor to test "only those controls necessary to obtain reasonable assurance about whether material weaknesses exist", then this statement appears to contradict that presumption. Appropriate process documentation for significant process should allow for adequate description of these lower risk controls, and therefore the walkthrough of these processes would cover these controls.

7. Is the proposed definition of "significant" sufficiently descriptive to be applied in practice? Does it appropriately describe the kinds of potential misstatements that should lead the auditor to conclude that a control deficiency is a significant deficiency?
The new definitions for deficiency, significant deficiency and material weakness are welcomed as this should help to reduce the scope, which is at least in part the intention of the amendments.
Page A1- 45 regarding the definition of control deficiency, we suggest adding: "misstatements in the financial statements".

8. Are auditors appropriately identifying material weaknesses in the absence of an actual material misstatement, whether identified by management or the auditor? How could the proposed standard on auditing internal control further encourage auditors to appropriately identify material weaknesses when an actual material misstatement has not occurred?
Giving indicators of material weaknesses is an interesting improvement. However, providing more examples of potential material misstatements concerning controls relating to the control environment, segregation of duties, how internal control over information technology affects this assessment, the ability to commit the company and deficiencies related in management override would help auditors to better understand and identify potential material weaknesses.

9. Will the proposed changes to the definitions reduce the amount of effort devoted to identifying and analyzing deficiencies that do not present a reasonable possibility of material misstatement to the financial statements?
By including a broad statement such as antifraud programs and controls in the guidance of what "results in at least a significant deficiency" may cloud the definition of significant deficiency as many transaction based controls, such as a bank reconciliation, contain antifraud aspects. In large entities with multiple locations, a control deficiency in one location related to such an antifraud control, presumably, would not constitute a significant deficiency neither for that entity nor for the group.

10. Should the standard allow an auditor to conclude that no deficiency exists when one of the strong indicators is present? Will this change improve practice by allowing the use of greater judgment? Will this change lead to inconsistency in the evaluation of deficiencies?
Due to the variety of possibilities and circumstance surrounding "strong indicators", we believe that the standard should allow the auditor to conclude that no "material weakness" exists when one of the strong indicators is present. Furthermore, the indicator relating to prior year restatements appears contradictory to the requirement to assess controls as of the balance sheet date. When the restatement is identified in the subsequent year, it appears that the control may be working properly in that year, and therefore the material weakness relates to the previous year's assessment.
One of the purposes of the new statement appears to be to allow for more auditor judgment, therefore, this would be consistent with the theme of the new standard.
We believe that the change would not lead to inconsistencies in the evaluations, rather inconsistencies in the outcome of the evaluations as the facts and circumstances surrounding each strong indicator are different, and cannot and should not be compared.

11. Are further clarifications to the scope of the audit of internal control needed to avoid unnecessary testing?
The scope appears appropriately outlined.

12. Should the reference to interim financial statements be removed from the definitions of significant deficiency and material weakness? If so, what would be the effect on the scope of the audit?
Making reference to interim financial statements in the definitions suggests that the timing of control testing should cover these periods (e.g. certain controls may need to be tested at each reporting period). As management's and the auditor's reports on the effectiveness are as of the balance sheet date, this inconsistency may result in additional testing or lowering the materiality considerations during the final assessment of the impact of deficiencies when interim materiality differs from overall materiality for the annual audit.

13. Will removing the requirement for an evaluation of management's process eliminate unnecessary audit work?
No, since global evaluation of management's process contributes to the overall evaluation of control environment. We consider that the quality of the management's process is a good indicator of the quality of internal control.
In fact, in certain situations it may increase the level of audit work. For example, currently the company's management and the auditors come to an agreement on the scope of the significant accounts and process to be tested as part of this evaluation process. If this process were eliminated, the need for agreement would be diminished thereby allowing management's scope to differ, maybe significantly, from that of the auditors. If the process or accounts considered significant by the auditors are not documented and tested by management, the auditors would be required to perform additional procedures in order to understand and assess these processes.

14. Can the auditor perform an effective audit of internal control without performing an evaluation of the quality of management's process?
Possibly, however, the efficiency of the audit may suffer due to considerations noted in the response to question 13.

15. Will an opinion only on the effectiveness of internal control, and not on management's assessment, more clearly communicate the scope and results of the auditor's work?
We believe that the current opinion adequately communicates the current requirements as it is a function of the standard. It doesn't appear to us that the mere inclusion of the opinion renders the scope of results of the auditors work any more difficult for the reader to understand.

16. Does the proposed standard appropriately incorporate the value of cumulative knowledge?
Generally speaking, yes. The use of prior results in considering the extent of testing is interesting. It is a little unclear in the guidance what effect previous testing has on a control and for how long reliance can be placed on it. Would, for example, a walkthrough determining that the control had not changed be sufficient or would testing need to be undertaken with a reduced sample size etc…? Although the standard should not aim to be prescriptive in all respects, more guidance in this area would be useful as it is already being debated by companies and, in our experience, also external auditors.

17. What are the circumstances in which it would be appropriate for the auditor to rely upon the walkthrough procedures as sufficient evidence of operating effectiveness?
For routine controls within significant processes which are unchanged from prior years. A mere walkthrough would not provide sufficient evidence relating to the operating effectiveness of complex non-routine controls in which high levels of judgment are concerned.

18. Will the proposed standard's approach for determining the scope of testing in a multi-location engagement result in more efficient multi-location audits?
Although the guidance is consistent with the risk based model, in practice it may be somewhat harder to implement. For example, a particular business unit may be within the testing scope due to its size and impact on the consolidated financial statements, however, it may consist of several, sometimes hundreds, of relatively small entities that, individually could be excluded from the scope.

19. Is the proposed standard's single framework for using the work of others appropriate for both an integrated audit and an audit of only financial statements? If different frameworks are necessary, how should the Board minimize the barriers to integration that might result?
We believe a single framework in appropriate.

20. Does the proposed definition of relevant activities adequately capture the correct scope of activities, including activities that are part of the monitoring component of internal control frameworks?
We believe it does.

21. Will requiring the auditor to understand whether relevant activities performed by others identified control deficiencies, fraud, or financial statement misstatements improve audit quality?
We believe that this is an essential component of relying on the work of others and is necessary to improve the quality of the audit.

22. Is the principal evidence provision that was in AS No. 2 necessary to adequately address the auditor's responsibilities to obtain sufficient evidence?
We don't believe so. In fact, by being able to review and rely on the works of other provides the auditor with valuable insight into key components of the over control environment. In certain circumstances, we have found that using the work of others, especially internal audit, may strengthen the external auditors own tests as generally the internal auditors have a vast knowledge of the company, its risk and its operating environment.

23. Does the proposed standard provide an appropriate framework for evaluating the competence and objectivity of the persons performing the testing? Will this framework be sufficient to protect against inappropriate use of the work of others? Will it be too restrictive?
The framework appears appropriate.

24. Has the Board identified the right factors for assessing competence and objectivity? Are there other factors the auditor should consider?
Generally yes, however, in certain cases the factors relating to education may be somewhat restrictive. For example, if the person does not have a degree in accounting or even a college degree, but has been an accounting manager in the industry for a significant period of time, this should be considered with the factor affecting competence within the framework.

25. What will be the practical effect of including, as a factor of objectivity, a company's policies addressing compensation arrangements for individuals performing the testing?
It adds a certain level of complexity to the evaluation as the auditors are required to assess the hierarchy of the compensation systems in place, which to a certain extent can be subjective. It also may limit the company's ability to utilize potentially highly efficient and effective tester who work within certain specific business lines within the organization.

26. Will requiring a walkthrough only for all significant processes reduce the number and detail of the walkthroughs performed without impairing audit quality?
Generally, significant processes contain several sub-processes for which the auditor must perform a walkthrough. If one of the sub-processes is not relevant to the assertions being tested, the auditor should have the ability to remove it from the scope. This should be appropriately addressed within the standard.

27. Is it appropriate for the auditor to use others as direct assistance in performing walkthroughs? Should the proposed standard allow the auditor to more broadly use the work of others in performing walkthroughs?
We believe that the standard appropriately limits the amount of assistance in performing the walkthroughs.

28. Does the proposed standard on auditing internal control appropriately describe how auditors should scale the audit for the size and complexity of the company?
The guidance does allow for some proportionality of controls depending on the size and complexity of the business, and this is to be welcomed. It is, however, difficult to place reliance on key controls that are not capable of demonstration, especially when this is combined with a reduction in the controls that are considered to be 'key'. Also, generally, as noted in the standard, smaller business rely on

significant management input in their day-to-day operations which significantly increase the risk of management override, limiting the auditor ability to place reliance on the controls. We are concerned that this, though good in theory, will prove difficult in practice.

29. through 33.
No specific comments.

34. How can the Board structure the effective date so as to best minimize disruption to on-going audits, but make the greater flexibility in the proposed standards available as early as possible? What factors should the Board consider in making this decision?
The Board should consider allowing for immediate adoption of the new standard. Although not all aspects of the new standard would be able to be fully utilized in the first year, the new definitions of significant deficiencies and material weakness along with the standards for assessment could be utilized in the first year.

Other comments

- Page A2-5 – Using the Work of Others - 10:
  we suggest to add in a) the nature **and timing**

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