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Sent: Monday, February 26, 2007 3:11 PM
To: Comments
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Subject: Society comments on proposals published in Release 2006-007

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via e-mail to: comments@pcaobus.org

February 26, 2007

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

Re: PCAOB Rulemaking Docket Matter No. 21

Proposed Auditing Standard – An Audit of Internal Control over Financial Reporting that is Integrated with an Audit of Financial Statements – and Related Other Proposals

Ladies and Gentlemen:
The Society of Corporate Secretaries & Governance Professionals is a professional association, founded in 1946, with over 4,000 members who serve more than 3,000 issuers. Responsibilities of our members include supporting the work of corporate boards of directors, their committees and executive management regarding corporate governance and disclosure. Our members ensure issuer compliance with the securities laws and regulations, corporate law, stock exchange listing requirements and the accounting rules, and have been on the front-line in implementing the structural changes necessitated by the Sarbanes-Oxley Act of 2002 and the related rules of the Securities and Exchange Commission, the Public Company Accounting Oversight Board (the "Board") and the exchanges. The majority of Society members are attorneys, although our members also include accountants and other non-attorney governance professionals.

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We commend the significant efforts by the Board to address issues previously raised by the Society and by others in the effort to balance improvements in the quality and efficiency of important corporate processes and controls against problems perceived and greater-than-expected costs incurred in the implementation of Auditing Standard No. 2. We join in the Board's view that "auditors should perform internal control audits as efficiently as possible for companies that are required by the SEC's rules to obtain an audit report on internal control", and we therefore commend the Board for undertaking an "evaluat[ion of] every significant aspect of the audit of internal control to determine whether the existing standard encourages auditors to perform procedures that are not necessary in order to achieve the intended benefits.". We generally support the measures proposed by the Board in its Release 2006-007 (the "Release"), as discussed below. Our comments include certain suggestions for additional flexibility without detracting from achievement of the goals articulated by the Board in the Release.

Generally, we support the Board's effort to design the proposals in the Release to focus the audit of internal control on those matters most important to internal control, to scale the audit for smaller companies subject to the audit requirement, and to eliminate procedures unnecessary for and simplify requirements relevant to the audit of internal control. Specifically, we support

1. incorporating into the standard proposed in the Release the top-down approach emphasized in the Board's May 16, 2005 guidance on applying Auditing Standard No.2, with a view to avoiding the auditors' reluctance to apply the prior guidance as somehow not consonant with Auditing Standard No. 2;
2. revising the definitions of the terms "significant deficiency" and "material weakness" to raise the threshold at which the likelihood of a misstatement is evaluated, to clarify that auditors are not required to search for deficiencies that, individually and in the aggregate, are less severe than material weaknesses, and to better establish the threshold of what is a significant deficiency; with a view to reducing the amount of effort, time and cost devoted to identifying and analyzing deficiencies that do not present a reasonable possibility of material misstatement to the financial statements;
3. aligning the standards of materiality in audits of internal control with the materiality standards long recognized as applicable to audits of annual financial statements, with a view to ending the differences between the materiality measures used to plan and perform the two audits;
4. permitting auditors to take into account knowledge obtained during prior audits, with a view to reducing the nature, timing and extent of testing based on the auditors' cumulative knowledge related to individual controls;
5. providing direction and approval, within the unified framework of a separate auditing standard, for auditors to use the work of others in an audit of internal control, with a view to removing impediments to use of the work of others that stem from particular provisions of Auditing Standard No. 2;
6. eliminating the requirement that auditors evaluate management's process for annual assessment of the effectiveness of the issuer's internal controls, with a view to avoidance of repetitive testing and to terminating what has been perceived to be inappropriate dictation by auditors of how management should perform its own assessment; and
7. deferring as to guidance for management to the (proposed) interpretive guidance published by the SEC in parallel with the Board's publication of the Release.

As to the recalibrated walkthrough requirements, we support the Board's decisions that the number of required walkthroughs can be reduced (based on significant processes rather than on major classes of transactions within each significant process) and that auditors can be allowed to utilize the direct assistance of others when performing required walkthroughs. We would, however, continue to recommend that the Board consider additional flexibility in allowing auditors to perform periodic walkthroughs, or to perform walkthroughs on a rotating basis, to the extent that auditor has appropriate reason to believe that the control involved has not changed since the last walkthrough. We agree that walkthroughs should be required for any process for which there has been a significant change during the fiscal year, but we do not believe that testing should be required annually for those controls that are highly automated, have not changed from the prior year and have given rise to no significant deficiencies in the past three years. Similarly, we suggest for Board consideration that the frequency of required walkthroughs even of "major transactions" be limited to every second or every third year provided, again, that the control has not changed in any significant manner and has given rise to no significant deficiencies in the past three years. This treatment of walkthroughs would reduce external audit costs to a meaningful extent and, perhaps more important, would enable issuers and auditors alike to focus the more on those controls which carry a greater element of risk.

We also believe that the existing guidance issued by the Board continues to be relevant and should be accorded specific recognition in the structure of the currently proposed guidance and the Auditing Standards proposed in the Release. Incorporating the existing guidance within the proposed new Auditing Standards would remove any ambiguity about the status of the prior guidance and ensure that it is honored in the dual audit process. We also suggest the importance of specific reference, in the proposed new Auditing Standards, to the management guidance ultimately issued by the SEC.

In addition, we believe it important that the Board monitor implementation by auditors of the definitive Auditing Standards that will replace Auditing Standard No. 2. The Board has consistently stated in guidance it has provided with respect to the audit of internal controls that it will focus its inspections on whether the auditors efficiently achieved the objectives of an internal control audit; continuance of that policy and monitoring of its implementation appears to us to be vital on a going-forward basis, and we would suggest that an explicit statement to that effect in the Board's release adopting the definitive Auditing Standards would be extremely useful.

Finally, we believe that the Board, like the SEC, needs to act promptly to complete and adopt its definitive standards implementing Section 404 of the Sarbanes-Oxley Act, in order to afford issuers subject to the requirements of those standards the ability quickly to enter upon implementation of all necessary changes as part of their audit preparations for fiscal 2007.

We appreciate this opportunity to share our views with you, and would be happy to provide you with further information to the extent you would find it useful.

Respectfully submitted,
The Society of Corporate Secretaries and Governance Professionals
Edward H. Fleischman
By: Edward H. Fleischman, Member of the Drafting Committee

cc: Lydia Beebe, Society Chairman-Elect
William Mostyn, Society Chairman
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