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

Re: PCAOB Rulemaking Docket Matter No. 021

Cisco Systems ("Cisco") appreciates the opportunity to provide our views on the Public Company Accounting Oversight Board ("PCAOB") proposed auditing standards, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements,* and *Considering and Using the Work of Others in an Audit* ("Proposed Standards").

Overall Observations

Cisco supports the Proposed Standards and their intent to assist auditors in making the audit process more efficient and cost-effective. We also appreciate the standard setting process whereby the audit requirements are further developed and refined in light of feedback from constituents and results from PCAOB examinations. We believe that the top-down, risk-based approach described in the Proposed Standards, will provide an opportunity for companies to work with their external auditors to develop an audit of internal control over financial reporting ("ICFR") that is more cost-effective and focused based on appropriate risk assessments. We also are supportive of the principles based approach which allows for an appropriate level of judgment to be exercised by auditors. We have included our observations and concerns herein regarding the Proposed Standards that we believe would help clarify certain of its provisions.

We believe that the Proposed Standards should be more closely aligned with the interpretive guidance for management proposed by the U.S. Securities and Exchange Commission ("SEC Guidance"). The level of detail in the Proposed Standards seems to be greater and more prescriptive as compared to the SEC Guidance. This could result in a misalignment of risk assessments and test plans between auditors and management which could result in inefficiencies and unnecessary costs.

To date, many companies' Sarbanes-Oxley Section 404 compliance approaches have been largely driven by the requirements set by external auditors. External auditors have been overly prescriptive in their requirements due to their perceived inability to apply judgment using a risk-based approach. Due to the absence of management guidance and an allowable risk-based approach, companies have been required to follow AS2 as well as strict interpretive guidance from the audit firms to satisfy the requirements of the integrated audit without the use of appropriate judgment. With proper alignment, the Proposed Standards and SEC Guidance should provide companies the flexibility to apply a top-down, risk-based approach using an appropriate level of judgment with external auditors being able to leverage a similar approach. We expect companies and auditors would focus their efforts on high risk areas achieving a better balance between internal control risk and the cost of compliance. Without alignment of the external audit standards and the SEC Guidance, companies would continue to focus efforts on the assessment of lower-risk control areas and incur additional costs failing to achieve the objective of a more risk-based and cost effective assessment.

We are also concerned that external auditors will need to be assured that the PCAOB examinations will align with the Proposed Standards. Consistent with the initial implementation of the AS2, auditors will be reluctant to adopt changes in their approach until sufficient PCAOB inspections of their firm's audits have occurred which will effectively result in a delayed implementation of the Proposed Standards. We encourage the PCOAB to provide auditors timely and sufficient guidance as to its inspection expectations under the Proposed Standards to allow for earlier realization of the benefits for both auditors and companies inherent in the Proposed Standards and SEC Guidance.

Other Observations

Top-down, Risk-based Approach

The risk assessment provisions in the Proposed Standards should allow auditors to eliminate excessive or redundant testing as well as for the varying of testing based upon prior knowledge of the company and audit results, as well as entity-level controls. The Proposed Standards include a description of risk factors in determining both significant account risk (paragraph 26) and operating effectiveness risk (paragraph 52). It is not clear from reading the note to paragraph 51 as to whether each control needs to be tested by the auditor. We are not clear whether the note is addressing all controls or those controls selected for testing. We believe that clarification on this point would be beneficial.

We believe that the Proposed Standards set the expectation that there would be one or a small number of controls for each combination of significant accounts and related assertions and that the auditors should test only those controls necessary to obtain reasonable assurance. More examples of the application of the top-down risk-based approach would be helpful to both management and auditors in order to strike the intended balance. This would be particularly helpful in the consideration of the interplay and balance of testing and reliance between entity and process level controls.

Rotational Testing

We support the focus in the Proposed Standards on the use of prior knowledge and audit results in the current year risk assessment and testing approach. The Proposed Standards allow for reduced testing in subsequent years based on the results of prior year testing and extent of changes in the controls. The Proposed Standards also allow for the benchmarking of automated controls. These approaches will result in increased efficiencies for both management and auditors resulting in lower compliance costs. We believe further efficiencies could be gained, without increasing risk, by allowing for the rotation of control testing. The current expectation of "each year standing on its own" would be required to be modified in order for this approach to be utilized. The rotation of controls should, of course, be based on an assessment of changes in controls, control design, prior year test results and the overall control risk.

Entity-level Controls

Companies that have put considerable effort in enhancing entity-level controls should be able to leverage these controls to reduce testing at the transaction level. Paragraphs 16 and 17 of the Proposed Standards indicate that a top-down approach begins with company-level controls, that those controls must be tested, and that the evaluation could result in increasing or decreasing other auditor testing. The Proposed Standards do not clearly indicate how the testing of company-level controls impacts the extent of other testing. We recommend that the PCAOB more clearly describe, using examples, how strong entity level controls and their testing can be used to reduce the extent of transactional level controls.

Assessment of Deficiencies

We are supportive of the change in the definitions of significant deficiencies and material weaknesses. The change from the "more than remote" likelihood criteria to "reasonable possibility" will provide greater clarity and reduce the time spent discussing internal control deficiencies. Additionally, the change in the significant deficiency definition from "more than inconsequential" to "significant" will also be similarly beneficial. These definitional changes along with the factors indicated in the Proposed Standards that should be considered will provide consistency in the identification and reporting of these deficiencies across companies and audit firms eliminating the need for firm specific criteria.

Interim Financial Statements

The definitions of "significant deficiency" and "material weakness" in the Proposed Standards include a reference to the misstatement of the company's "annual or interim financial statements." The SEC Guidance indicates that, "As part of the evaluation of ICFR, management considers whether the deficiencies, individually or in combination, are material weaknesses as of the end of the fiscal year". The assessment of ICFR under Section 404 of the Sarbanes Oxley Act is an annual process designed in order to make a determination as of the end of a company's fiscal year as to the effectiveness of its controls. Consequently, the reference to the "interim financial statements" in these definitions seems inconsistent with that objective. We recommend that the reference to "interim financial statements" be removed with the focus limited to the annual financial statements.

Removal of Opinion on Management's Assessment

We do not expect to see substantial efficiencies result from the removal of the opinion on management's assessment as companies will continue to have a need to align their assessment process with those of their auditors. However, we do believe that the opinion should be eliminated as it does not provide any further assurance to investors. The removal of the opinion will provide companies the choice and ability to develop assessment processes that are tailored to their control environments.

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We are supportive of the Proposed Standards and SEC Guidance. We would encourage the PCAOB and SEC allow for their implementation as soon as possible in order to realize their benefits providing for a more efficient and effective audit process. We appreciate the opportunity to comment on the PCAOB's proposed auditing standards. Please feel to contact me at (408) 527-0448 for any further discussion of our comments.

Sincerely,

Jonathan Chadwick
Vice President, Corporate Controller, Principal Accounting Officer