

April 28, 2006

Nancy M. Morris  
Secretary  
U. S. Securities and Exchange Commission  
100 F. Street, NE  
Washington, DC 20549-1090

***Re: File 4-511, Feedback on Implementation of Sarbanes-Oxley Internal Control Provisions***

Caterpillar Inc. would like to thank the Securities and Exchange Commission for the opportunity to comment again this year on our experiences regarding compliance with the provisions of Section 404 of the Sarbanes-Oxley Act of 2002 ('the Act').

For more than 80 years, Caterpillar Inc. has been building the world's infrastructure and, in partnership with Caterpillar dealers, is driving positive and sustainable change on every continent. With 2005 sales and revenues of over \$36 billion, Caterpillar is the world's leading manufacturer of construction and mining equipment, diesel and natural gas engines and industrial gas turbines. More information is available at <http://www.cat.com/>.

Over the years, Caterpillar has proudly built a solid reputation as a highly ethical company. We recognize and fully endorse the important roles companies such as Caterpillar play in maintaining public confidence in Corporate America, including our responsibility to ensure an effective system of internal controls. Accordingly, we continue to support, in principle, the Commission's goal of enhancing the effectiveness of internal control over financial reporting.

Moving into year three of our compliance with the Act, we have experienced both positive and negative aspects of the Act and believe there are areas for improvement going forward.

### **Positive Aspects:**

- **Higher recognition within management of their responsibility for internal controls** - While Caterpillar management has always maintained a high standard of ethical behavior and strong internal controls over financial reporting, the Act has helped to bring about a higher recognition of management's responsibility for the control environment. There is clear recognition among our business leaders of the importance of the internal control environment and their accountability for ensuring their business units are compliant with the requirements of the Act.
- **Higher involvement of Audit Committees** – While Caterpillar's Audit Committee reflected many of the standards now required for many years, we believe the Act has helped increase the focus of Audit Committee members across the board. Further, all of our Audit Committee members are considered financial experts, as defined. We believe the intent of the Act has worked well in application.
- **Board independence** – Caterpillar has over the years maintained a strong and independent Board of Directors. All of Caterpillar's Board members, except for the Chairman, are non-executives.
- **Strong tone at the top** – Caterpillar is proud of our reputation as a highly ethical company. Our Code of Conduct was first issued in 1974 and was recently updated to reflect our values. Caterpillar has also maintained a whistleblower protection program and has established a world-class business risk management process.

### **Areas for Improvement:**

- **The Act continues to focus on details vs. high-risk areas** – The financial scandals by a few companies, which the Act was intended to deal with, did not occur at the transactional level, but were the result of unethical leaders and weak governance. Tone at the top and entity level controls, in our opinion, is where the focus of Section 404 compliance should be, not at the detailed transaction level. Although we achieved many efficiencies and

reduced our Section 404 compliance costs in year two, we continue to feel that the current interpretation of the Act is causing focus on retesting transactional controls (i.e., looking for signatures on detailed transactions) vs. the bigger picture of management tone. In many respects, this is a rules-based approach, whereas a principles-based approach is what is truly needed. By focusing on the principles of high integrity financial reporting and the surrounding control environment rather than detailed testing of transactions, the intent of the Act could be realized at a lower burden to the issuers. Furthermore, by placing undue emphasis on transaction controls, there is a risk that areas of higher risk are overlooked.

- **Fear of using judgment by the audit firms** – A frequent message during last year’s SEC Roundtable was that audit firms should exercise judgment in their application of Section 404. While PCAOB reviews of audit firm performance in year one of compliance with the Act have to date been conducted behind closed doors, there appears to be a much different message being given to audit firms – one of having to prove the judgment they have taken. We are concerned this inconsistent message causes unneeded conversation within the audit firms and raises costs to issuers. Audit firms need to be able to exercise professional judgment without fear of reprisal or second-guessing.
- **The five-year rotation rule for audit partners is onerous** – The current requirements of rotating audit partner’s needs to be changed and we recommend a return to the previous seven-year rotation. For a complex, global company like Caterpillar, it takes the audit partner the first one to two years to be able to fully and efficiently understand Caterpillar and the complex environment we operate in (over 200 facilities in a highly integrated organization). The acceleration of partner rotations also adds to the complexity of matching skills to client audit environment, allowing appropriate transitions, as well as issues associated with relocating and resettling families in many instances. We believe five years is simply too short for an effective partner rotation, causing issuers to bear this cost of inefficiency and creating a higher degree of risk as a result of partner rotations. Seven years makes more sense from a transition standpoint and, in our opinion, achieves adequate assurance of partner independence.

**Conclusion:**

Caterpillar continues to support good corporate governance, including tone at the top, independence of the Board and whistleblower protection. We believe there have been some benefits derived from Section 404. However, significant costs have been placed on U.S. companies to comply with Section 404, primarily from the transactional focus of Section 404. Additionally, audit firms are fearful of how their good judgment used in their audits will be viewed by PCAOB. And finally, the five-year partner rotation needs to be extended to seven years to optimize the knowledge and benefit from the experience of the audit partner.

We are hopeful the Commission will reevaluate interpretations of Section 404 and welcome the opportunity to discuss these issues at your convenience. Please contact me at (309) 675-4212 or Mr. Ned Neuhaus at (309) 675-4210.

Sincerely,

Ali M. Bahaj