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July 26, 2019

Ms. Vanessa Countryman  
Secretary  
U.S. Securities & Exchange Commission  
100 F Street N.E.  
Washington, DC 20549

**Re: File No: S7-06-19; Amendments to the Accelerated Filer and Large Accelerated Filer Definitions**

Dear Ms. Countryman:

Deloitte & Touche LLP is pleased to respond to the Securities and Exchange Commission's request for comment on the proposed *Amendments to the Accelerated Filer and Large Accelerated Filer Definitions* (the "Proposed Amendments"). Our comments focus on the effect of the Proposed Amendments on the requirements related to companies' internal control over financial reporting (ICFR).

Chairman Clayton noted in his statement at the open Commission meeting on the Proposed Amendments that the Sarbanes-Oxley Act of 2002 has made our capital markets "a place where Main Street investors have a high degree of confidence in the quality of the financial statements and other financial disclosures they receive from our public companies."<sup>1</sup> We agree, and we believe investors have greatly benefited from the reforms put in place by Sarbanes-Oxley, including the requirements related to ICFR.

We have observed that, since the requirements for management reporting on ICFR and the related requirement for the audit of ICFR were put into place, they have contributed greatly to, among other things:

- increased accountability of individuals involved in all aspects of the financial reporting process;
- more effective corporate governance practices;
- reduction in the number of material financial statement restatements;
- reduced risk of fraud; and
- overall enhanced reliability of audited financial statements.

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<sup>1</sup> Available at <https://www.sec.gov/news/public-statement/statement-clayton-050919>.

The SEC staff has emphasized the benefits of ICFR by underscoring its importance in the successful implementation of new accounting standards, including those on revenue recognition, leasing, and current and expected credit losses (CECL).<sup>2</sup>

Further, we believe that in the 15 years since the implementation of the requirement for an audit of ICFR under Section 404(b) of Sarbanes-Oxley, those audits have become much more efficient and effective. This has happened as issuers and auditors have become more experienced with evaluating the design and testing the operating effectiveness of ICFR. The efficiency and effectiveness of ICFR audits also have been aided by the PCAOB's revised *Auditing Standard 2201: An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*; guidance issued by the PCAOB and SEC;<sup>3</sup> as well as materials published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).<sup>4</sup>

Because of the demonstrated benefits of Section 404(b), we do not believe it would be prudent to roll back existing requirements for a large population of issuers that are currently complying with Section 404(b). We recognize, however, that in fulfilling its mission, the SEC must consider whether the investor protection mechanisms of this safeguard may be less critical—or even serve as a barrier to entry—for some companies. As the Commission notes in the release accompanying the Proposed Amendments, Congress and the SEC have already made such distinctions related to Section 404(b) with regard to certain groups of companies. Given this, and the fact that the thresholds relevant to accelerated filer status have not changed in more than 15 years, we support the limited additional exemptions from Section 404(b) that would come with the Proposed Amendments, because they appear to strike a reasonable balance between the SEC's investor protection and capital formation missions.

We do, however, have a few observations that may be relevant as the Commission considers its next steps on the Proposed Amendments.

If the Proposed Amendments are adopted, it is important that both companies and their investors have a clear understanding of how the auditor's role in reviewing ICFR will change for companies that are newly exempt from Section 404(b). As noted in the release, auditors are required to consider ICFR as part of the financial statement audit, even when a company is exempt from Section 404(b). For example, the auditor is required by PCAOB AS 2110: *Identifying and Assessing Risks of Material Misstatement* to "obtain a sufficient understanding of each component [of ICFR] to (a) identify the types of potential misstatements, (b) assess the factors that affect the risks of material misstatement, and (c) design further audit procedures."<sup>5</sup> This understanding includes

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<sup>2</sup> See Wesley R. Bricker, Chief Accountant, [Statement in Connection with the 2017 AICPA Conference on Current SEC and PCAOB Developments](#) (December 4, 2017) ("over the next several years internal controls will be particularly important as companies work through the implementation of the significant new accounting standards. Well-run public companies have effective internal controls not just because internal controls are a first line of defense against preventing or detecting material errors or fraud in financial reporting, but also because strong internal controls are good for business and can have an impact on costs of capital.... If left unidentified or unaddressed, internal control deficiencies can lead to lower-quality financial reporting which can ultimately lead to higher financial reporting restatement rates and higher cost of capital").

<sup>3</sup> See PCAOB [Staff Views-An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements: Guidance for Auditors of Smaller Public Companies](#) (January 23, 2009); [Commission Guidance Regarding Management's Report on Internal Control Over Financial Reporting Under Section 13\(a\) or 15\(d\) of the Securities Exchange Act of 1934](#) (June 27, 2007).

<sup>4</sup> See, e.g., *Internal Control over Financial Reporting — Guidance for Smaller Public Companies* (2006), which was superseded by its updated [Internal Control-Integrated Framework \(2013\)](#) and its [Internal Control over External Financial Reporting: A Compendium of Approaches and Examples \(2013\)](#). See also COSO's *Guidance on Monitoring Internal Control Systems* (2009).

<sup>5</sup> AS 2110.18, available at: <https://pcaobus.org/Standards/Auditing/Pages/AS2110.aspx>.

evaluating the design of the controls relevant to the audit and determining whether the controls have been implemented.

From an investor expectation perspective, it is important that investors understand that, while audits of newly exempt companies will still involve ICFR, as noted above, the auditor will not be required to test the operating effectiveness of such controls, nor will it be issuing an opinion on the effectiveness of those controls. While the PCAOB's new auditor reporting model mitigates potential investor confusion on this point by requiring disclosure by the auditor when the company is exempt from Section 404(b),<sup>6</sup> if it adopts the Proposed Amendments, the Commission should take care not to inadvertently increase investor confusion on this point.

From a cost perspective, we expect that reductions in audit hours that some may anticipate due to exemption from the requirement to perform testing of the operating effectiveness of ICFR may be partially offset by an increase in audit efforts necessary for a standalone financial statement audit. For example, where an auditor previously may have been able to rely on controls it tested to reduce the extent of substantive testing in an integrated audit, it may now need to increase the amount of substantive testing to complete the standalone financial statement audit. Alternatively, when moving to a financial statement only audit, the auditor may decide upon an audit strategy that relies on controls to reduce the extent of substantive testing; in that case, the auditor would still need to perform tests of operating effectiveness of some controls. Therefore, the effect that the Proposed Amendments may have on total audit fees will be facts and circumstances dependent.

As noted above, while we support the limited exemptions from Section 404(b) that would follow from the Proposed Amendments, we do not believe broader exemptions are warranted. We are aware, however, that the limited group of companies that would be exempt if the Proposed Amendments are adopted are not the only ones that have expressed concern about the costs of compliance with Section 404 of Sarbanes-Oxley. We therefore believe that the SEC should continue to support efforts to ensure that the requirements of both Section 404(a) and (b) are clear and scalable for companies of varying size and complexity.

While the PCAOB, SEC and COSO in the past each issued guidance intended to emphasize the scalability of Section 404,<sup>7</sup> refreshed guidance may be helpful, especially to guide management about its responsibilities. That could, in turn, enable the auditor to tailor its audit procedures to be more efficient. We note that there are some efforts already underway in this area, including the Financial Executives International's (FEI) recent guides on internal control considerations for companies' adoption of the new leasing and the CECL standard, which are intended to "help companies of varying sizes execute successful implementation and maintenance of effective ICFR for these new standards."<sup>8</sup>

We encourage the SEC to continue to support this and other focused efforts, as well as encourage more multi-stakeholder conversations designed to improve the effectiveness and efficiency of both management's assessment and the audit of companies' ICFR.

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<sup>6</sup> In that circumstance, the auditor must state in its opinion that, while management is required to report on the company's ICFR that report is not required to be audited, and the auditor has not been engaged to perform an audit of management's assessment of the effectiveness of ICFR. PCAOB AS 3101: *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion* (2017).

<sup>7</sup> See *supra* notes 3 and 4.

<sup>8</sup> Available at <https://www.financialexecutives.org/About-FEI/For-the-Press/2018/FEI-Releases-Guides-to-Help-Navigate-Internal-Cont.aspx>.

We appreciate the opportunity to provide our perspectives as the Commission considers the Proposed Amendments. We would be happy to discuss further any of the points in our letter. If you have any questions, or would like to discuss our views further, please contact Christine Davine at [REDACTED].

Sincerely,

*Deloitte & Touche LLP*

Deloitte & Touche LLP

cc: Jay Clayton, Chairman  
Robert Jackson, Jr., Commissioner  
Hester Peirce, Commissioner  
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Allison Herren Lee, Commissioner  
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