



September 18, 2006

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Nancy M. Morris  
Secretary  
U.S. Securities and Exchange Commission  
Station Place  
100 F Street, N.E.  
Washington, DC 20549-9303

Re: Comments to Concept Release Concerning Management's Reports on Internal Control over Financial Reporting

Dear Ms. Morris:

Thank you for providing the opportunity to comment to the Securities and Exchange Commission ("SEC") in response to its Concept Release Concerning Management's Reports on Internal Control over Financial Reporting ("Concept Release" or "Release"). The Financial Services Roundtable ("the Roundtable") represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Roundtable member companies provide fuel for America's economic engine, accounting directly for \$50.5 trillion in managed assets, \$1.1 trillion in revenue, and 2.4 million jobs.

***Opening Comments:***

Roundtable member companies believe strong corporate governance and transparency of management structure and internal controls are crucial for a dynamic and sound economy. However, our companies continue to struggle with implementation of the requirements of Sarbanes-Oxley, ("SOX" or "the Act") Section 404 and we have outlined below several recommendations to improve the process.

We believe that clearer guidance from the SEC is required to reduce unnecessary costs to business by eliminating some of the excess and duplicative assessments of internal controls. For example, Roundtable member companies are concerned about the changing roles of auditors. Due to the potential liabilities created under the Public Company Accounting Oversight Board's ("PCAOB") Auditing Standard No. 2, auditors are now reluctant to advise clients or interpret the Act.

External auditors have also increased the scope of testing and request excessive documentation during audits due to the same concerns. In addition, there is some confusion over the interpretation of key terms such as "material weakness" and "significant controls."

The Roundtable supports meaningful controls of a public company's systems of financial reporting to ensure investor protection. We will continue to aggressively lobby the Congress and regulators to improve the effectiveness and reduce the costs associated with the SOX Section 404 internal control over financial reporting.

***Specific Recommendations:***

The Roundtable has developed the following set of recommendations based on input from our members. Later this month, our executives are meeting to continue, among other things, to develop policies and best practices for effective internal control evaluation and reporting. While we anticipate that there may be minor changes and additions, what follows are suggested reforms that we ask be affirmatively considered:

1. Make Amendments to SOX 404 Implementation

- Require a risk-based, three-to-five year audit cycle with annual testing of the critical, high-level, entity-wide internal controls.
- Require a "base year" or full Section 404 audit every three-to-five years to include revenue recognition, significant transactions and subsidiary account reviews.
- Allow base-year testing to be followed by annual, limited testing of critical, high-level entity-wide controls in other or "off" years.
- Allow limited three-to-five year cyclical testing ONLY if there are: (1) no material weaknesses; (2) no restatements required and (3) no fraud is found.
- Companies could be given the choice of "opting in" or maintaining their current systems.

2. Issuance of a More Forceful Policy Statement

For regulatory consistency, as well as for better guidance for filers, the SEC should consider issuing a new, more forceful policy statement on internal control reporting, similar to the statement it adopted in 1981, following passage of the

Foreign Corrupt Practices Act (“FCPA”). That SEC statement provided, in pertinent part:

- The test of the internal control system is whether, taken as a whole, it reasonably meets the statute’s specified objectives.
- Reasonableness, as a standard, includes a consideration of feasibility. One measure of reasonableness of a system relates to whether the expected benefits from improving it would be significantly greater than the anticipated costs of doing so. Thousands of dollars should not be spent conserving hundreds.
- Considerable deference should be afforded to the company’s reasonable business judgments. The selection and implementation of particular control procedures, so long as they are reasonable, remain managements’ prerogatives and responsibilities.
- The accounting provisions principal objective is to reach knowing or reckless conduct, not inadvertent conduct.
- Corporate management and the board have important roles to play in monitoring and evaluating the adequacy of internal controls, but not involvement in the minutia or recording and accounting for every transaction.

### 3. Permit Reliance on the Work of Others

Auditing Standard No. 2 has been interpreted in such a way as to prevent significant reliance on the work of a company’s internal auditors or outside regulators (NASD, SEC, FED, etc.) While the PCAOB has clarified that this is not the objective for low-risk areas, the requirement still exists for an auditor to perform his own work in “high risk” areas. Section 404 should be amended to allow an independent public accounting firm to rely significantly on the examinations and inspections conducted by Federal and state regulatory agencies to the extent appropriate.

### 4. Conduct Complete Evaluation of Compliance Costs

There have been two recent, highly divergent studies released regarding costs for Section 404:

FEI Study in March, 2006, showed the cost of compliance with Section 404 for the average public company was reduced by 17 percent from 2005, but still remains high at approximately \$3.7 million per company.

A contemporaneous CRA Study found compliance expense reductions of 44 percent for large cap companies and 31 percent for small cap companies.

The experience of our members does not support the extent of compliance-cost reductions contained in either the FEI or CRA findings. It may be appropriate to conduct a more comprehensive SEC-sponsored study of Section 404 costs.

#### 5. Relaxation of Restriction on Communications with Auditors

For the internal controls review required by Section 404 to be useful to a company, Section 404 should be amended to allow management of the company to communicate openly with the independent public accounting firm about the nature, scope, and structure of its internal controls without adversely affecting the independence of the firm for purposes of fulfilling its attestation function.

#### 6. Promote Competition and Eliminate *de minimis* Conflicts

There exists a “logjam” of conflicts that has arisen with only four large accounting firms capable of servicing the larger public issuers. The SEC and the PCAOB should take all reasonable steps to increase the number of qualified accounting firms and to eliminate *de minimis* conflict of interest provisions.

### ***Conclusion***

As discussed above, the Roundtable urges the Commission to consider the following recommendations:

- Make Amendments to SOX 404 Implementation
- Issue a More Forceful Policy Statement (as with FCPA)
- Permit Reliance on the Work of Others
- Conduct Complete Evaluation of Compliance Costs
- Relax Restriction on Communications With Auditors
- Promote Competition and Eliminate *de minimis* Conflicts

The Roundtable looks forward to working with the Commission on these important matters to improve internal control reporting. If you have any questions concerning these comments, or would like to discuss these issues further, please

contact Mitzi Moore, at [mitzi@fsround.org](mailto:mitzi@fsround.org) or 202-589-2424 or me at rich@fsround.org or 202-589-2413.

Sincerely,

*Richard M. Whiting*

Richard M. Whiting  
Executive Director and General Counsel

cc: Chairman Christopher Cox  
Commissioner Paul S. Atkins  
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Commissioner Cynthia A. Glassman  
Commissioner Annette L. Nazareth  
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