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March 31, 2005

Mr. Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609.

Re: File Number 4-497

Dear Mr. Katz:

Intel Corporation is pleased to have the opportunity to provide feedback regarding the implementation of Section 404 of the Sarbanes Oxley Act (the "Act"). We appreciate the SEC's willingness to consider opportunities to improve existing guidance to enable both effective and efficient internal control testing and reporting.

Intel fully supports management accountability for maintaining effective internal control over financial reporting. Section 302 certifications, Section 404 internal control reports, and enhanced penalties under the federal sentencing guidelines work together to promote the accuracy and reliability of public company disclosures. Ultimately, these elements will have the most far-reaching effects in combating the fraudulent financial reporting practices that precipitated passage of the Act.

We also recognize the positive benefits Section 404 has had in heightening controls awareness and improving the rigor of internal control procedures; however, we believe these same benefits could be realized with a more balanced, cost-effective approach to implementation. A March 2005 survey conducted by Financial Executives International ("FEI") put the average cost of year-one compliance for companies with greater than \$25 billion in revenue at approximately \$15 million.¹ Even though Intel embarked on Section 404 compliance with a long history of strong internal control and an excellent governance rating from GovernanceMetrics International,² our investment level still exceeded FEI's \$15 million figure. While the absolute cost was substantial, the real issue is the wholly disproportionate cost relative to the benefits.

¹ Press Release, FEI, Companies Say Section 404 Improves Investor Confidence, But Question Cost vs. Benefit; Suggest Improvements (Mar. 21, 2005), http://www.fei.org/files/spacer.cfm?file_id=1498.

² Brendan Intindola, *22 Companies Win Perfect Rating for Governance*, FORBES, Feb. 9, 2004, available at <http://www.forbes.com/reuters/newswire/2004/02/09/rtr1251406.html>.

Relative to the potential risk of material misstatement, companies expended excessive effort documenting and testing routine transaction processing and information technology controls.

We believe the disproportionate cost is largely driven by unintended consequences of Public Company Accounting Oversight Board (“PCAOB”) Auditing Standard No. 2, *An Audit of Internal Control Over Financial Reporting Performed in Conjunction With an Audit of Financial Statements* (“Standard No. 2”). These same unintended consequences could prevent costs from declining appreciably in future years. However, the following refinements to existing guidance could considerably reduce costs, without, in our view, diminishing the efficacy of Section 404.

1. Promote A Risk-Based Approach to Testing and Documentation:

While the SEC’s rules allow for flexibility based “on the circumstances of the company and the significance of the controls,”³ the prescriptive nature of the Standard No. 2 coupled with conservative interpretation deters both management and auditors from taking a managed, risk-based approach to Section 404.

First, Standard No. 2 unduly restricts the ability of companies and auditors to rely on accumulated learning. “[E]ach year’s audit must stand on its own. Therefore, the auditor must obtain evidence of the effectiveness of controls for *all* relevant assertions for *all* significant accounts and disclosures *every year*.”⁴ While testing all relevant assertions for all significant accounts is a practical way to establish the implementation year baseline, the standard fails to recognize the value of cumulative knowledge in assessing potential risk. Such restrictions are inconsistent with a risk-based model, which would allow for modulation of the frequency and scope of testing based on the strength of the underlying control environment and accumulated learning. Additionally, the bar on rotation ignores the fact that many controls, particularly in the information technology area, remain unchanged from year to year.

We recommend the SEC issue guidance that would provide the means for management to take a risk-based approach to Section 404 and for auditors to assess management’s approach accordingly. Specifically, we request the SEC and PCAOB allow both companies and auditors to rotate testing where there is a proven strong control environment and where control points are structured and continuous (e.g. application and routine transaction controls). Rotation is a well-established practice in auditing literature⁵ and is a practical alternative that not only continues to provide investors with a high level of assurance, but also allows management and auditors to focus greater attention on higher risk areas.

³ Final Rule: Management’s Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, Securities and Exchange Commission Release Nos. 33-8238, 34-47986, IC-26068, 68 Fed. Reg. 36643 (June 18, 2003).

⁴ PCAOB Release No. 2004-001, Standard No. 2, 15 (Mar. 9, 2004) (emphasis added).

⁵ See, e.g., *Due Professional Care in the Performance of Work* (AICPA, *Professional Standards*, vol. 1, AU § 230) (“The independent auditor’s objective is to obtain sufficient competent evidential matter to provide him or her with a reasonable basis for forming an opinion. The nature of most evidence derives, in part, from the concept of selective testing of the data being audited, which involves judgment regarding both the areas to be tested and the nature, timing, and extent of the tests to be performed.”); *Consideration of Internal Control in a Financial Statement Audit* (AICPA, *Professional Standards*, vol. 1, AU § 319) (“Because of the inherent consistency of IT processing, the auditor may be able to reduce the extent of testing of an automated control.”).

Second, Standard No. 2 places an inordinate emphasis on documentation, classifying inadequate documentation as at least a deficiency and potentially a significant deficiency or material weakness.⁶ However, as stated in the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) Framework: “Many controls are informal and undocumented, yet are regularly performed and highly effective. . . . The fact that controls are not documented does not mean that an internal control system is not effective, or that it cannot be evaluated.”⁷

The current documentation requirements create a layering effect of conservative interpretation and an undue emphasis on verifiability by third parties. Auditors facing the prospect of the new and unfamiliar PCAOB inspection process conservatively interpret Standard No. 2. Management then reacts to this conservatism by creating more documentation than would otherwise be warranted to assure the auditor’s standards will be met or exceeded. The end result is conservatism on top of conservatism.

Instead of a rigid rule, we recommend companies be given flexibility to tailor the form of the documentation to their unique circumstances and auditors be allowed to exercise professional judgment in evaluating the adequacy of documentation.

2. Eliminate the Redundant Internal Control Effectiveness Opinion:

The Act requires auditors to “attest to, and report on, the assessment made by the management.”⁸ However, Standard No. 2 requires not only that auditors opine on management’s assessment but also separately opine on the effectiveness of the company’s internal control over financial reporting.⁹ Furthermore, the auditor must rely on its own work to provide the “principal evidence” for its conclusion.¹⁰ This separate opinion and its principal evidence requirement leads to an unnecessary level of duplicative testing.

We recommend that consistent with Congressional intent as expressed in the Act, the auditor attest to management’s assessment, not render a redundant internal control opinion. To conclude on management’s assessment, the auditor will still need to perform sufficient attest procedures to reduce to a low level the probability of not discovering materially misstated assertions. The level of testing, however, would not be as extensive as that required to independently opine on the effectiveness of the design and operation of controls. This cost-sensitive approach will allow the auditor to satisfy its obligation to validate management’s assessment and will still encourage management to develop quality documentation and test procedures.

Alternatively, we request that the principal evidence requirement be relaxed. Auditors should be able to apply professional judgment to modulate reliance consistent with the caliber of management’s work. Where management has performed a quality assessment supported by

⁶ PCAOB Release No. 2004-001, Standard No. 2, A-24 (Mar. 9, 2004).

⁷ COSO, *Internal Control-Integrated Framework* 73 (1994).

⁸ Sarbanes-Oxley Act of 2002 §404(b), Pub. L. No. 107-204, 116 Stat. 745.

⁹ PCAOB Release No. 2004-001, Standard No. 2, A-72 (Mar. 9, 2004).

¹⁰ *Id.* at A-47.

competent, independent testing, the auditor should have the flexibility to rely more heavily on the work of others.

3. Encourage Appropriate Auditor Communication:

We believe more guidance is necessary to distinguish between what would constitute an auditor functioning in a control capacity versus a natural progression of financial statements from preliminary drafts to final filing readiness. The communication approach advocated in PCAOB guidance is unduly cumbersome, with companies required to communicate the (1) precise stage of financial statement completion at each step along the way; (2) “extent of controls that had operated or not operated” as of that point in time; and (3) “purpose for which the company was giving the draft financial statements to the auditor.”¹¹ Instead of adopting a formulaic approach to communication, new guidance should promote the ultimate objective of improving the accuracy and reliability of financial statements in the hands of investors.

Additionally, while it has not been Intel’s experience, we are cognizant that other companies have experienced overly conservative interpretation of auditor independence rules, stifling valuable communication about the appropriate application of complex technical accounting matters. While management should make the ultimate decision on the appropriate accounting treatment, discussing possible alternatives with auditors promotes the Act’s objective of improving financial reporting. The PCAOB’s attempt to address the issue of auditor communication through question and answers, while helpful, is insufficient.¹² Instead, we recommend the SEC and PCAOB affirmatively support appropriate dialogue between auditors and companies on complex accounting matters.

4. Support a Holistic Approach to Reporting Requirements:

The SEC is currently considering accommodations for small issuers. While we appreciate the unique challenges faced by small issuers in supporting Section 404 compliance, we are also mindful that many of the control issues occur at small companies. According to 2004 disclosure statistics compiled by Compliance Week, over three-fourths of the issues occur at companies with less than \$1 billion in revenue.¹³ Thus, we would encourage the SEC to take a holistic

¹¹ PCAOB Staff Questions & Answers, *Auditing Internal Control Over Financial Reporting*, 6 (June 23, 2004).

¹² The PCAOB noted that “[a] discussion with management about an emerging accounting issue that the auditor has recently become aware of, or the application of a complex and highly technical accounting pronouncement in the company’s particular circumstances, are all types of timely auditor involvement that *should not necessarily* be indications of weaknesses in a company’s internal control over financial reporting.” *Id.* at 7 (emphasis added). While companies can now take comfort that a deficiency determination is not automatic, companies and auditors may still err on the side of curtailing the dialogue given the possibility it could be construed as a deficiency.

¹³ Presentation by Scott S. Cohen, Editor & Publisher, COMPLIANCE WEEK, *Analysis Of Weakness And Deficiency Disclosures, 2004*, available at http://www.fei.org/files/spacer.cfm?file_id=1443. Compliance Week’s findings are comparable to those in COSO’s study of fraudulent financial reporting. “Relative to public registrants, companies committing financial statement fraud were relatively small. The typical size of the sample companies ranged well below \$100 million in total assets in the year preceding the fraud period. Most companies (78 percent of the sample) were not listed on the New York or American Stock Exchanges.” COSO, *Fraudulent Financial Reporting: 1987-1997 - An Analysis of U.S. Public Companies*, available at <http://www.coso.org>.

approach to reducing the costs for all issuers, while still allowing for some level of rigor for small companies.

Additionally, in the interest of full transparency, we encourage the PCAOB and SEC to make inspection reports and auditor financials publicly available. Finally, we recommend that PCAOB inspections evaluate not only the effectiveness of auditor's procedures, but the efficiency of the overall audit process.

Conclusion:

In closing, we would like to reinforce that Intel fully supports the letter and spirit of the Act. While Section 404 has contributed to enhanced internal control over financial reporting, those benefits have come at great cost. Now that companies have spent the past 24 months preparing for and complying with Section 404, it is time to step back and holistically evaluate the effort, cost, and effectiveness of implementation relative to the Act's original intent. Adopting a practical and adaptive approach based on experience will yield significant benefits without compromising investor protection.

Thank you for consideration of our views. Please do not hesitate to contact me at (503) 696-7931 if you would like any further information in connection with our comments.

Sincerely,

/s/ James G. Campbell

James G. Campbell
Vice President
Corporate Controller