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Australia's First Bank

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

31 March 2005

Re: File Number 4-497

Dear Mr Katz

We would like to thank you for the opportunity to comment on our experience with the implementation of Section 404 of the Sarbanes-Oxley Act of 2002 ("SOX S404").

By way of background, Westpac Banking Corporation ("Westpac") is one of the four major banking organisations in Australia and also one of the largest banks in New Zealand. We provide a broad range of banking and financial services in these markets, including retail, commercial and institutional banking and wealth management activities. As at 30 September 2004, our market capitalisation was USD 25 billion (AUD 32 billion).

Overall, we support the objectives of SOX S404 of improving the accuracy and reliability of corporate disclosures. However, our experiences with implementing SOX S404 have highlighted areas where we consider the cost of compliance does not meet the benefits in the most effective way possible. It is in this spirit that we offer the following observations.

1. Focus of SOX S404

The corporate collapses that led to the enactment of SOX S404 appear to have been largely a result of ethical lapses, collusion and overall "tone at the top" issues. These issues are normally highlighted through application of the control environment component of the COSO framework, rather than through detailed process analysis.

The importance of focus on company-level controls, rather than process-level controls, appears to be supported by market commentators and rating agencies. In particular, we highlight an extract from a Moody's report[1] analysing SOX S404 weaknesses:

> "We are less concerned about material weaknesses that relate to controls over specific account balances or transaction-level processes. We refer to these material weaknesses as "Category A" material weaknesses. In most cases, we believe that the auditor can effectively "audit around" these material weaknesses by performing additional substantive procedures in the area where the material weakness exists. We expect to give companies reporting Category A material weaknesses the benefit of the doubt and not take any related rating action, assuming management takes corrective action to address the material weakness in a timely manner."

[1] Moody's Investors Service Global Credit Research Special Comment paper dated October 2004 titled: "Section 404 Reports on Internal Control: Impact on Ratings Will Depend on Nature of Material Weaknesses Reported".

Our experience has been that the effort required to comply with SOX S404 tends to be weighted more towards process-level controls as opposed to pervasive controls operating across the organisation. In our view, this approach is an outcome of applying PCAOB Auditing Standard No. 2 *An Audit of Internal Control Over Financial Reporting Performed in Conjunction with An Audit of Financial Statements* ("PCAOB Auditing Standard No. 2") which is directing external auditors (and therefore management) to focus their efforts on documenting and testing process-level controls.

We recommend that PCAOB Standard No. 2 be reviewed to refocus greater effort on the control environment and less emphasis on documentation and testing of process level controls.

2. Risk based approach to management and auditor testing

We note that PCAOB Standard No. 2, paragraph 126 acknowledges that external auditors may "to a large extent (perhaps entirely)" rely on the work of others in areas such as fixed asset depreciation where controls "…are usually not pervasive, involve a low degree of judgment in evaluating their operating effectiveness, and can be subjected to objective testing… so long as the degree of competence and objectivity of the individuals performing the test is at an appropriate level." However, PCAOB Standard No. 2 does not allow for documentation and testing of these low risk areas to be reduced.

In our view it would be far more effective to allow a risk-based approach to the testing of the operational effectiveness of controls by both management and external auditors to ensure that effort is focused on those areas with a higher inherent risk of material misstatement.

For example, in the case of fixed asset depreciation noted above, if during the first year of compliance management has found that the key controls over this process are both designed and operating effectively, we believe that the frequency and nature of operational effectiveness testing in subsequent years could be reduced to allow management to focus on areas of higher inherent risk. Reduced testing could include reliance on a control self-assessment process, or limiting detailed review of the process to a more infrequent rotational basis, such as every three years. We believe that applying a wider risk-based approach to testing would give rise to a more streamlined outcome with efforts focussed on more critical areas.

3. Auditor reliance on control self-assessment processes

PCAOB Standard No. 2, paragraph 126 notes that the external auditor should not rely on control effectiveness testing performed by management "because such an assessment is made by the same personnel who are responsible for performing the control, the individuals performing the self-assessment do not have sufficient objectivity as it relates to the subject matter."

Our understanding is that external auditors cannot place reliance on an internal control self-assessment ("CSA") process, unless the work is performed (or re-performed) by an independent area within a company. We believe that this will have the undesirable outcome of reducing management's ownership of and involvement in the control environment and possibly increasing the cost incurred.

We recommend that the PCAOB consider amending this requirement to allow external auditors to place reliance on a CSA process in instances where there are sufficient controls in place over the CSA process to provide assurance on the results of management's testing. We believe that a well-controlled CSA environment would include:

- An appropriate governance framework including an escalation process to the Board of Directors;
- Appropriate training of staff in relation to CSA activities;
- Clearly articulated monitoring activities which are linked to financial reporting control objectives;
- Documentation of monitoring activities sufficient to allow for re-performance;
- Verification of the sufficiency of the monitoring activities by an independent function and testing (validation) of CSA results by an independent function; and
- Sufficient and timely reporting of the results of CSA activities.

4. Legacy systems

In order to meet the requirements of SOX S404, we understand that it is required that we test and prove calculations within critical applications. To do this properly represents a significant commitment of both effort and funding.

A number of these applications are legacy systems that have been in place for many years and have been subject to decades of management, internal and external audit review.

To reduce the cost of compliance, we recommend that a risk-based approach be allowed for legacy systems that focuses on the assessment and testing of incremental change or recent development work.

5. Off balance sheet activities

There has been very little guidance provided in relation to the extent to which controls over off balance sheet activities should be included in management's assessment of controls over financial reporting. Two exceptions are the specific discussion of trust accounts and a response to a Frequently Asked Question in relation to compliance with laws and regulations.

We would appreciate additional guidance on this matter, as the interpretation will have a significant impact on the scope of management's control assessment activities.

6. Safeguarding of assets

Similarly, there has been very little guidance provided in relation to safeguarding of assets. In particular, our external advisors believe that this requirement could be as far reaching as covering all aspects of asset management from the physical controls over cash to the controls over optimisation of investment decision-making processes.

We would appreciate additional guidance in relation to the extent to which safeguarding of assets should be addressed under SOX S404.

We would be pleased to provide you with any further information necessary to assist you in reviewing this submission.

Yours sincerely

Margaret Payn
General Manager Group Finance
Westpac Banking Corporation