May 14, 2004

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

Re: PCAOB-2004-03

Dear Mr. Katz:

Dominion is one of the nation's largest producers of energy, with an energy portfolio of about 24,000 megawatts of generation, 6.4 trillion cubic feet equivalent of proved natural gas reserves and 7,900 miles of natural gas transmission pipeline. Dominion also operates the nation's largest underground natural gas storage system with more than 960 billion cubic feet of storage capacity and serves 5.3 million retail energy customers in nine states and have more than 400,000 shareholders.

In response to the Securities and Exchange Commission's (Commission) April 8, 2004 notice soliciting public comments on Public Company Accounting Oversight Board (PCAOB); Notice of Filing of Proposed Rule on Auditing Standard No. 2, *"An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements"* (Proposed Rules), Dominion Resources, Inc. (Dominion) hereby submits the comments on the topics listed below:

- Cost of Compliance
- Material Weakness and Adverse Opinion
- Scope Limitations
- Delay of the Effective Date

Dominion strongly believes in good corporate governance and understands the intent of Congress when it passed the Sarbanes-Oxley Act of 2002 (Act). We also believe the Proposed Rules need to strike the right balance between the obligations and burdens placed on public companies and their auditors, and the needs of investors and the Commission to have assurances that corporate internal controls are effective.

Cost of Compliance

Currently, Dominion, like many other registrants, is expending a considerable amount of time, money and resources to comply with Section 404 of the Act (Section 404). Total costs of first-year compliance with Section 404 of the Sarbanes-Oxley Act could exceed $4.6 million for each of the largest U.S. companies, according to a survey of 321 companies by Financial Executives International. While the PCAOB went into great detail about the awareness of the cost of compliance issue in the Proposed Rules, in their comments to their commissioners, and in the briefing paper, their actions did little to truly address the issue. We believe that there are some small modifications that the Commission can make to the Proposed Rules that would greatly reduce the annual cost of compliance and would have minimal effect on the quality of the overall attestation. Listed below are suggested adjustments to the Proposed Rules:

- **Rotational Testing of Controls**

  Allow rotational testing of controls over significant cycles and applications by management and their auditors under the following conditions:

  - The annual evaluation of the control environment demonstrates a strong control environment with low fraud risk factors;
  - Financial reporting controls over all significant cycles or applications have been evaluated and tested during a recent period of no more than 3 years;
  - Management and the auditors test on different rotational schedules; and
  - No specific reporting or risk issues preclude the use of rotation.

- **Reliance on Work Performed by Others**

  Allow greater reliance on work performed by others. The Proposed Rules attempted to address this issue by allowing auditors to use the work of others and were based on the same concepts as Statement on Auditing Standards ("SAS") No. 65, "*Auditor's Consideration of the Internal Audit Function in an Audit of the Financial Statements"*. However, the Proposed Rules create an overall boundary on the use of the work of others by requiring that the auditor's own work provide the "principal evidence" for their audit opinion. Currently, the "large public accounting firms" have interpreted the "principal evidence" language to require that they must perform at least sixty-six percent of the audit work to reach their opinion. Many registrants have dedicated significant resources to achieve a high level of audit expertise in their internal audit departments. If an internal audit department is evaluated to be both highly competent and objective, as described in SAS No. 65, it would seem appropriate to rely on more than one-third of their total work effort.

We believe that some simple clarifying language about the principal evidence language in the Proposed Rules is necessary to allow for more reliance on the work performed by others.

- **Walkthroughs**

  We believe that the requirement for the auditor to perform walkthroughs in each annual audit of internal control over financial reporting should not be mandated. The stated objective in the Proposed Rules is for the auditor to obtain an understanding of internal controls over financial reporting. We believe that this mandated audit step is overly prescriptive and creates a large burden on the auditor's time and thus adding additional cost to registrants. A walkthrough is a useful device for understanding a new business process, but it assumes the auditor is not familiar with a process. An auditor, who is familiar with a process, can obtain an understanding of the internal controls using many methods. We believe that the use of corroborative inquiry is a more effective and more efficient method for obtaining this understanding when the auditors are knowledgeable about the internal controls over a process because of past audit experience. However, should an auditor who chooses to use walkthroughs to validate that the key controls in a process have not changed since they were last audited should be allowed to reduce the extent of their control testing. The Proposed Rules should allow auditors, when conducting control testing, to use more discretion when determining the appropriate scope, frequency, and types of procedures. Mandated audit procedures simply drive up the cost of compliance and add little value to the quality of the overall attestation

Material Weakness and Adverse Opinions

The Proposed Rules require an adverse opinion if a material weakness exists as of year-end. We do not believe it is appropriate that the existence of one material weakness at year-end should automatically require management and the auditor to express an adverse conclusion about the effectiveness of the company's internal controls structure. Registrants and their auditors will encounter situations where a qualified "except for" conclusion would be more appropriate. For example, a qualified "except for" conclusion would seem more appropriate in situations where a material weakness has an isolated impact on the overall effectiveness of internal control over financial reporting. If available, a qualified opinion in this example would provide more meaningful information to investors and the Commission about the extent and nature of a specific internal control problem. An adverse opinion should provide a signal of the magnitude of a pervasive weakness in internal controls.

Scope Limitations

Dominion believes that a limit in the scope of Section 404 assessments should be allowed when management does not have the authority to affect, and therefore cannot assess, the controls in place in certain instances. This would relate to entities that are consolidated or proportionately consolidated as well as non-affiliated entities. Due to the magnitude of the work effort and costs associated with the Section 404 assessments, the PCAOB or the Commission must set some general guidelines with respect to the scope of the assessment with the release of these final rules. Without clear boundaries, registrants and their auditors will be left to determine the scope of their assessment for themselves, and eventually the PCAOB or the Commission will be forced to step in because of divergence in practice.

The simple answer to the issue of internal controls outside the authority of management has been the suggestion that the company obtain a Statement of Auditing Standard No. 70 Type II Report, "*Report on Controls Placed in Operation and Tests of Operating Effectiveness*" (SAS 70). However, this simple answer has some serious challenges. For example, many registrants are just now realizing the extent of their internal controls that have been outsourced to other non-affiliated companies that haven't been considered a "traditional" service organization in the past. Many of these organizations have never had a SAS 70 audit before, and it is doubtful that there are currently a sufficient number of qualified auditors, both internal and external, to perform SAS 70 audits, year-end financial audits and Section 404 audits. Additionally, some of these registrants have entered into these contractual relationships where the right to audit the internal controls of the service organization does not exist and to amend their contractual relationships at this late hour may not be practical.

Below we present two examples that further illustrate the complexities of this issue. We believe that the Commission must act to address this issue at the same time the Proposed rules are adopted.

Example 1: Many registrants are spending considerable amount of time and resources to implement Financial Accounting Standards Board Interpretation No. 46 (FIN 46), *Consolidation of Variable Interest Entities.* Registrants are finding that in some cases they are unable to obtain the information necessary to even record theses entities on their books. Even if this information is available and it can be recorded, in many cases management still lacks the authority to affect the controls at these entities. We believe that if a registrant cannot obtain the information necessary to assess an entity's internal controls, and/or lacks the authority to affect the controls of these entities, it would seem appropriate to limit the scope of the Section 404 assessments.

Example 2: Many States have created energy choice programs to facilitate utility competition. Under these programs, customers receive one bill from their local utility. However, a new energy supplier replaces the local utility as the supplier of their energy, while the local utility continues to deliver the energy, read meters, collect payments, provide service and respond to emergencies. Under these programs, some of the energy supplier's key controls over their revenue accounts are under the supervision and control of a non-affiliated company. In many cases, these suppliers lack the authority to audit these key controls, or even to request that an audit be performed over these key controls. It would seems appropriate under these circumstances, and in similar situations, that management's Section 404 assessment be limited to only the internal controls that they have authority to affect, and that are under their supervision.

Delay of the Effective Date

We believe a delay in the effective date of the Proposed Rules, consistent with the timing of the issuance of the final rules by the SEC, is necessary to provide additional time for registrants and their auditors to adjust work already completed for any changes made to the proposed standard and to adequately develop testing plans. Assuming the SEC adopts the final rules by the end of June, this leaves registrants with calendar year-ends and their auditors less than six months to interpret and comply with these rules. Accordingly, we recommend that the Section 404 reporting requirements be effective for fiscal years ending after June 15, 2005.

Dominion appreciates the opportunity to comment to the Commission. Thank you for considering our views. We would be happy to discuss them with you in further detail.

Respectfully submitted,

Steven A. Rogers
Vice President, Controller and
Principal Accounting Officer

Filed: May 14, 2004