

# FULTON FINANCIAL

## CORPORATION

ONE PENN SQUARE • LANCASTER, PENNSYLVANIA 17602

May 10, 2004

Jonathan G. Katz  
Secretary  
U.S. Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549

**Re: PCAOB Rulemaking: Public Company Accounting Oversight Board; 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," Release 34-49544; File No. PCAOB-2004-03 issued April 8, 2004 (the "Proposed Standard").**

Dear Mr. Katz:

I appreciate the opportunity to comment on the above referenced Proposed Standard. As a chief audit executive having more than 30 years' experience evaluating the effectiveness of internal control structures, including controls over financial reporting, I find the 'alpha and omega' of the Proposed Standard troubling. During my career I have been integrally involved in setting standards for the internal auditing profession through my membership on The Institute of Internal Auditors' Internal Auditing Standards Board. In my role as a past President of the National Association of Financial Services Auditors, which is now the Financial Services Audit Group of The Institute of Internal Auditors, I have also been a strong advocate for the proper design and implementation of internal controls. It is in the capacity of chief audit executive and management team member that I express concern with the §404 implications presented by the Proposed Standard. The comments that follow are mine and mine alone and do not necessarily represent the views of the senior management of Fulton Financial Corporation.

Having had to comply with the Federal Deposit Insurance Corporation Improvement Act (FDICIA) of 1991 since 1991, I am integrally familiar with the work effort required to opine on the effectiveness of the internal control structure on an annual basis. While FDICIA was initially promulgated as having minimal burden on reporting, it has been shown to be quite the opposite. One could easily argue the value of complying with FDICIA has been negligible. With regard to §404, the work effort required to document processes, identify significant risks and mitigating controls, evaluate control design and effectiveness and report on such effectiveness of internal controls on an annual basis has already been extremely time-consuming and, by extension, costly. Although certain improvements and refinements have been incorporated in the Proposed Standard, the costs will still be significant and excessively disproportionate to the value gained. It is inconceivable that a standard such as this could have been proposed without regard to rigorous cost/benefit analyses.

I am concerned with the exhaustive scope of the required audit procedures and their associated prohibitive costs. Audit fees have already increased exponentially with no ceiling in sight. Not only has this become a lucrative revenue enhancement opportunity for the external auditors, it has also become a virtual money pit for registered companies. Unlike government entities, deficit spending is not a viable option for public companies. The Financial Executives International organization has estimated companies over \$5 billion will incur \$1.4 million in external consulting fees, software acquisition charges, etc. In addition, fees for the external auditors' opinions on internal controls are expected to be 33% to 40% of the financial statement audit fees. I have heard estimates that fees could actually be exponentially higher than financial statement audit fees. With the big four accounting firms auditing over 90% of reporting companies, the likelihood is practically zero that competitive pressures will reduce these costs.

Mr. Jonathan G. Katz, U.S. Securities and Exchange Commission  
May 10, 2004  
Page 2

The PCAOB and others have indicated that the benefits of these internal control audits include improving public confidence in our financial reporting system and preventing business and financial reporting abuses and/or failures, e.g., Enron. While public confidence may improve via these audits, I seriously question whether they will be a remedy for business and financial reporting abuses and/or failures. It is impossible to legislate corporate morality; yet, that appears to be the expected deliverable. I believe it is a widening and disturbing misconception that audits of internal controls will eliminate business and financial reporting failures. There will always be ethically challenged and morally bankrupt chief executives. This Proposed Standard will not change that.

With the financial and reputation risk events surrounding the Arthur Andersen debacle, the public accounting profession is, understandably, overly cautious regarding public company engagements. This cautionary approach has resulted in extreme inflexibility regarding what is and what is not acceptable for documenting and testing the controls over the financial reporting process. This inflexibility has run the gamut of documenting all risks and controls over financial reporting processes regardless of significance, to documenting all risks and controls regardless of financial statement impact. The public accountants, because of the power they now wield with respect to rendering opinions on internal controls, have effectively been given carte blanche regarding fees charged. That is not a condemnation of the public accounting profession; rather, it happens to be the result of the Proposed Standard.

As one might expect, the attestation work required by the external auditors has taken on a life of its own. Having reread §404, specifically paragraph (b), the outside auditor is required to attest to management's assertions regarding the effectiveness of internal controls over financial reporting. "Any such engagement shall not to be the subject of a separate engagement." When Congress mandated that the outside auditors attest to management's report, it was fully aware that professional standards already existed to guide practitioners in performing the engagement. Although the PCAOB was given authority to revise those attest standards, creating an entirely new engagement is clearly not indicated in §404(b). In effect, the PCAOB may very likely have gone beyond or even disregarded what Congress intended.

I urge the SEC to reconsider the cost of implementing this standard in terms of management resources and audit fees. A much more critical evaluation of this Proposed Standard's value is needed, i.e., who is intended to benefit from this Proposed Standard, how will that benefit materialize and is the cost offset by the value attained. Additionally, I urge the SEC to reconsider the effective date of these requirements. Having no more than six months from the date of this Proposed Standard to document and test all controls over the relevant assertions related to all significant accounts is an unnecessary burden brought on by the PCAOB's delay in issuing the Proposed Standard. The public accounting firms are even struggling to address the questions and issues raised by the Proposed Standards. This Proposed Standard, in whatever final form, should be implemented properly and carefully. Expedience should not be the goal. Lastly, I encourage the SEC to revisit the timeliness issue with regard to SAS70 reports received from third party service providers. For reviews completed with an effective date within the bounds of acceptable reliance, receipt of such reports will often occur subsequent to the year-end assessment date. In order to receive and evaluate a SAS70 report prior to the assessment date, the effective date would be too early for reliance. I contend that any SAS70 report with an effective date in the same year as management's assertion would be timely enough for reliance, especially since these third party providers must also comply with §404 requirements for assertion and attestation purposes.

Thank you for the opportunity to comment on the Proposed Standard and for considering the views expressed in this letter.

Respectfully submitted,

