17 September 2006

Ms. Nancy M. Morris, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Subject: Concept Release Concerning Management's Reports on Internal Control Over Financial Reporting (Release No. 34-54122; File No. S7-11-06)

Dear Ms. Morris

I appreciate the opportunity the SEC offers for comments about the Concept Release noted above. The discontent with the implementation of SOX continues. The need to reshape the related regulations is critical to the maintenance of an optimum financial environment in the United States, as well as in the world community.

The SEC is to be applauded in its efforts to redress the problems that have arisen. In a brief article (September issue of THE CPA JOURNAL) a colleague and I wrote of some perceived flaws in the implementation of the 2002 Act by the PCAOB. The haste with which the PCAOB made judgments about the tasks they would assume, including taking on the audit standard setting role and requiring two audits under Section 404, now in hindsight appear not to have been wise. The need for a new type of oversight was clearly required; the passage of SOX was a wise decision.

I shall not be responding to the specific questions raised in the Concept Release. Noted in the Introduction was the following: ". . . the Commission deems it necessary to issue additional guidance for management on its assessment of the effectiveness of internal control over financial reporting. We currently anticipate that the guidance issued would be in the form of a rule, which would address the topics that we have outlined. . . . "

The type of specific guidance implied in the series of questions raised in the Concept Release seems inappropriate. There are varied environments in which internal control exists. The range of possible strategies available in the design and oversight of internal controls for a particular entity precludes specification in meaningful fashion.

Some very simple questions come to mind:

1. What guidance should the SEC provide? Is it not sufficient that the SEC establish the objectives to be achieved in an entity's implementation of internal controls? While objectives are universal, the manner in which they are met varies considerably.

> The U S. Government, through a variety of initiatives, especially following the Employment Act of 1946, has encouraged economic growth. As I read the details of this Concept Release, I began to *imagine* that the SEC became concerned about

how companies could enhance their profitability: "What would the SEC say – in its guidance – about what companies should do to improve their profitability?"

Would it not be as difficult to tell public companies how they should enhance profitability as it is to now to tell them how to set up their internal controls, assess them, and then maintain documentation?

The SEC should merely state the objectives for internal controls. Possibly, an updated statement of Sec. 101 of the Foreign Corrupt Practices Act of 1977 would be sufficient. The outcome anticipated from adequate internal controls can be stated clearly and would be applicable to all sizes and types of entities. Some general principles might be developed to enhance the operational understanding of the objectives.

2. Isn't the goal to increase the assurance that financial reporting will have greater validity and reliability than is perceived to be the case after the disclosures of a cascade of alleged audit failures during the last decade?

Is it not time to recognize that the unending request for "more guidance" on the part of both companies and public accounting firms is surprising and possibly not warranted? Could the uncertainty about what should be done be a strategy of subterfuge? If a person totally unacquainted with professional accounting/ auditing literature were to read many of the comment letters to the two Roundtables, such a person would conclude that internal control is a new concept.

3. Why were the revisions to auditing standards that clearly stated auditor responsibility for internal control seemingly unheeded in the process of performing audits?

It may be too late for a thorough diagnosis of failure related to internal control. However, possibly, some astute investigations may be needed to gain better insight into the type of regulatory oversight required to assure adherence to a quality internal control environment. The questions that should be addressed should dwell on what must be done to be assured that companies are **actually doing** what they have been reporting for more than two decades in their annual reports about maintaining internal controls. (Such disclosure was voluntary before the recent SOX-related disclosures, but many companies provided such a disclosure) Furthermore, what oversight will **assure adherence** to long standing guidance on the part of external auditors?

Internal control is not a new concept. In the 70s, there were thoughtful reports, for example, including *The Commission on Auditors' Responsibilities: Report, Conclusions, and Recommendations (known as the Cohen Report)* which was the outcome of 66 monthly meetings, beginning in 1975. The Report was issued in 1978. Another report issued by the AICPA in September 1978 was *Tentative Report of the Special Advisory Committee on Accounting Control.* Many additional sources of guidance have been issued since these illustrative reports of approximately three decades ago.

4. Are two audits required? In fact, is either of these audits as separate tasks necessary?

Should it not be sufficient for management to acknowledge its responsibility, etc? Possibly, there needs to be more disclosure by the external auditor related to internal control. (I am not sure how this should be designed at this point . .)

An integrated audit makes sense in today's world and the significance of *integrated* needs further exploration. Possibly, external auditors should be required to consider the audit of internal control a component of their financial audits and add a phrase to that effect in the standard report. If there are serious inadequacies in internal control, there should be a scope limitation or a disclaimer of opinion with sufficient disclosure of the problem(s).

5. How effective is the strategy for inspections?

First, there should be a reconsideration of the combination of audit standard-setting *and oversight*. This combination raises a number of serious questions about the wisdom of the Board's decision to be the standard setter. (this was not a requirement of SOX.)

The task of oversight is comprehensive and is sufficient scope for an oversight board. It appears that the inspections are more effective than were the peer reviews in earlier years. Yet, the dual responsibility and the nondisclosure policy of segments of the inspection reports both deserve objective review at this time.

It is clear that oversight was unbelievably ineffective earlier and SOX is clearly justified. Possibly, the PCAOB can continue to assume the oversight responsibility. However, a review of the PCAOB to date is needed. The SEC has the talent and commitment to objectively provide such a review.

A clarification of objectives relative to responsibility for internal control by management and by auditors should be sufficient as related to what is being proposed in the Concept Release. I hope that the SEC will reconsider the appropriateness of this Concept Release.

Sincerely

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