November 21, 2003

Office of the Secretary
PCAOB
1666 K Street, N. W.
Washington, D.C. 20006-2803

RE: PCAOB Rulemaking Docket No. 008

Dear Sir or Madam:

Commercial Federal Corporation (CFC) welcomes the opportunity to comment on the PCAOB's proposed auditing standard "An Audit of Internal Control over Financial Reporting Performed in Conjunction with an Audit of Financial Statements," as referred to in Section 404(b) of the Sarbanes-Oxley Act of 2002 (SOX). This comment letter is in direct response to the PCAOB Rulemaking Docket Matter No. 008.

CFC's primary subsidiary is Commercial Federal Bank (CFB). CFB is a $13 billion federal savings bank, headquartered in Omaha, Nebraska, and regulated by the Office of Thrift Supervision. CFB operates 192 branches across seven states, including Arizona, Colorado, Iowa, Kansas, Missouri, Nebraska, and Oklahoma. CFB has been subject to the provision of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) since its inception. And, specifically as it relates to SOX Section 404, FDICIA Section 112 since 1993.

We applaud the efforts of the PCAOB (the Board) as a major contributor to the landscape of enhanced governance and accountability investors rightfully expect. The Board's efforts to help restore credibility to integrity of corporate America's financial reporting processes and improve the associated oversight provided by the public accounting profession is definitely warranted. However, although we are all disheartened by the highly visible corporate misdeeds that resulted in the Sarbanes-Oxley legislation, we must also remember that overlaying excess burden and cost on the infrastructure of corporate America penalizes no one other than consumers and shareholders in the long-run. While good controls are, and should always be, cost-effective over the long-term, unnecessary and excessive validation, verification and duplication is cost-prohibitive and not in anyone's best interests. Caution should be exercised before we fully chastise the many by the misdeeds of the few through unnecessarily and onerous rules. Maybe unfortunately, but realistically, we cannot legislate, regulate or standard set corporate misfeasance and malfeasance out of existence. And, in an era of increasingly complex and evolving accounting rules, unintended restatements of financial results will undoubtedly continue.

The most troubling aspects of the proposal revolve around:

- the unwarranted and over-reaching transformation of the **attestation** of management's assessment of the effectiveness of internal control over financial reporting to an **audit** of internal control over financial reporting,
- the presumption that because there may have been some isolated instances of over-reliance on the work of others for banks under FDICIA results in a virtual elimination of any substantive reliance, and
- the inherent conflict of interest that gets created by having the auditors evaluate the audit committee.

The proposed standard solicits commentary on 31 specific questions. Contained below are our thoughts on those that we respectfully request the Board to revisit and/or reconsider:

1. Is it appropriate to refer to the auditor's attestation of management's assessment of the effectiveness of internal control over financial reporting as the audit of internal control over financial reporting?

Response to Question 1:
The words in SOX Sections 103 and 404 require the auditor to "present an evaluation," "provide reasonable assurance," "contain an assessment of the effectiveness," and "attest to, and report on." A review of most any widely recognized dictionary will draw a distinction between an "audit" and an "attestation." An attest engagement has traditionally been distinguished from an audit. Congressional intent seems to be that an attestation be performed, not an audit. Furthermore, this is what was also the intent of FDICIA and, as has been often quoted, the intent of SOX in this context was to closely mirror FDICIA. And, lastly, even the SEC recently signaled this distinction in its implementing release on SOX Section 404 by referring to the auditor's report on management's assessment as an attestation report (not an audit report) which is to be made in accordance with standards for attestation engagements. Therefore, we believe that the guidance should not outline how to perform an audit of controls, but rather should be implementing congressional intent by focusing on how to properly evaluate management's assertion. If the Board does not consider revision of the standard and extend the opportunity for the auditor to perform a more measured and appropriate assessment of the process leading to management's assertion, whereby greater reliance can be placed on the work of others, then the auditor's extensive work/testing as outlined in the proposal ("control environment" controls, "period-end" controls, information technology "general controls, walkthroughs, significant nonroutine transactions, significant accounts, etc.) does become an audit.

4. Does the Board's proposed standard give appropriate consideration to how internal control is implemented in, and how the audit of internal control over financial reporting should be conducted at, small and medium-sized issuers?

Response to Question 4:
The issue is more of complexity, level of centralization, sophistication and amount of outsourcing, than solely an issue of size. How an auditor determines what the key controls over financial reporting are, and limiting the work to solely key controls, will be the primary factor. Where these key controls resultantly reside (centrally or decentrally, nationally or internationally, inside the company or outsourced, etc.) drives the complexity of the auditors work. The proposed standards suggests that "For a smaller, less complex company, the Board expects that the auditor will exercise reasonable judgment in determining the extent of the audit of internal control and perform only those tests that

are necessary to ascertain the effectiveness of the company's internal control." Is that not the case regardless of the size or complexity? Shouldn't the auditor exercise the same judgment taking into account all factors at any company?

8. Is it appropriate to state that inadequate documentation is an internal control deficiency, the severity of which the auditor should evaluate? Or should inadequate documentation automatically rise to the level of significant deficiency or material weakness in internal control?

Response to Question 8:
If management's documentation of the design of the internal controls and/or management's documentation supporting their assessment of internal control effectiveness is deemed to be inadequate by the auditor, that alone should not result in a de facto significant deficiency or material weakness. If adequate controls exist and the auditor can validate or otherwise determine such existence, even in the absence of adequate documentation, then there may not be a significant deficiency or material weakness. However, if due to the inadequacy of documentation, the control cannot be validated or otherwise determined to exist, then the facts and circumstances should drive whether there is a significant deficiency or material weakness. In coming to this conclusion, we need to be sure we are remembering the audience we are communicating to and what they want and/or need to know. We must also remember that the proposed standard suggests that a repeat significant deficiency would rise to the level of material weakness in a subsequent period if not cured in a reasonable time. Does an investor, reading management's assertion in concert with the auditor's attestation report, need or ever really care to know that there was a control documentation concern but otherwise the "financial results are fairly presented in all material respects?" Unless the documentation inadequacy would result in more than a remote possibility of material misstatement, does this really add any valuable information for the investing public? (See response to question #17 regarding the definition of significant deficiency.)

10. Is it appropriate to require that the walkthrough be performed by the auditor himself or herself, rather than allowing the auditor to use walkthrough procedures performed by management, internal auditors, or others?

Response to Question 10:
Walkthroughs are certainly a valid and legitimate audit evidence gathering technique, and judiciously applied, can be useful in testing a process and the associated controls. The auditor should determine what financial statement accounts and disclosures are worthy of testing by the use of a walkthrough technique, but there should be certain facts and circumstances where reliance on the work of others can be deemed to be acceptable. For instance, if a company's internal audit function had completed walkthroughs, and that internal audit function's work is determined to be independent and reliable, the auditor should first conduct selected reperformance tests. Assuming the internal auditor's work is assessed as reliable, then the auditor should be able to accept the remainder of the internal auditors walkthrough evaluation without performing any further work on his or her own. Completely dismissing the work of others in this instance, however, seems to be an unnecessary and overly burdensome (and cost ineffective) stance.

Importantly, however, walkthroughs are not always necessary. The focus should be on testing how management made their assessments, and performing tests as required to gain assurance regarding management's assessment process and the associated conclusions. These tests may or may not require the extensive walkthroughs currently specified in the proposed standard.

11. Is it appropriate to require the auditor to obtain evidence of the effectiveness of controls for all relevant assertions for all significant accounts and disclosures every year or may the auditor use some of the audit evidence obtained in previous years to support his or her current opinion on management's assessment?

Response to Question 11:
We do not believe the concept of rotation of testing or evaluation makes inherent sense. If each year's management assertion and auditor attestation needs to stand on its own for the fiscal year being reported on, then each key control should be evaluated annually. To entertain the concept of rotation would call into question whether the controls being evaluated were key or critical controls, rather than supporting or secondary controls. The evaluation should only concern itself with key or critical controls that could, in their absence or failure, result in the potential for material financial reporting errors or restatements.

12. To what extent should the auditor be permitted or required to use the work of management and others?
13. Are the three categories of controls and the extent to which the auditor may rely on the work of others appropriately defined?
14. Does the proposed standard give appropriate recognition to the work of internal auditors? If not, does the proposed standard place too much emphasis and preference on the work of internal auditors or not enough?
15. Is the flexibility in determining the extent of reperformance of the work of others appropriate, or should the auditor be specifically required to reperform a certain level of work (for example, reperform tests of all significant accounts or reperform every test performed by others that the auditor intends to use)?
16. Is the requirement for the auditor to obtain the principle evidence, on an overall basis, through his or her own work the appropriate benchmark for the amount of work that is required to be performed by the auditor?

Response to Questions 12, 13, 14, 15, 16:
The proposed standard defines three categories of controls and the extent to which the auditor may use the work of others for each category. These categories result in either a conclusion of "no reliance," "limited reliance," or "no limitations on reliance." However, the proposed standard also goes on to state that the auditor's own work must provide the principal evidence for the audit opinion. The interplay of these principles seems to result in very little reliance on the work of others in most any area of potential materiality. Even though there are no specific limitations on reliance on the work of others in areas of routine processing of significant accounts, how does the work become the principal evidence for the audit opinion without extensive independent work by the auditor or extensive reperformance work? The proposal seems to be building in a lot of redundant cost by not allowing greater reliance on the work of others. Once the auditor is done with:

- personally testing and evaluating all significant control environment controls,
- personally testing and evaluating all significant period-end financial reporting controls,
- personally testing and evaluating all significant pervasive controls (e.g., information technology general controls),
- personally conducting all necessary walkthroughs,
- personally assessing in some manner all controls over significant nonroutine and nonsystematic transactions, and

- personally assessing in some manner all significant accounts, processes, or disclosures,

what is there left to do of a material nature?

A highly qualified, competent, and independent internal audit function, duly assessed as such by the auditor, should result in a comfort level on the work they perform. This should, in turn, allow for a much greater reliance on the work of that internal audit function than the standard currently proposes. Acknowledging this in the standard will signal what is already true: the work of a competent and objective internal audit function is cost effective and can be relied upon to a great extent.

17. Will the definitions in the proposed standard of significant deficiency and material weakness provide for increased consistency in the evaluation of deficiencies? How can the definitions be improved?

Response to Question 17:
The proposed standard's definition for significant deficiency is problematic. The determination of the deficiency as significant needs to be based on a multitude of factors beyond just the interpretation of the interplay of the concepts of "remote" and "inconsequential." Under the current proposal, any control weakness which could potentially (not actually) result in an error that is not inconsequential, would result in a significant deficiency. What does inconsequential mean? The dictionary defines it as "not relevant" or "of no importance." It seems that the threshold is set too low for "significance" -- anything that is more than not relevant or beyond no importance? The category of significant weakness should only include those weaknesses with enough importance to warrant the attention of the audit committee.

22. Is it appropriate to require the auditors to evaluate the effectiveness of the audit committee's oversight of the company's external financial reporting and internal control over financial reporting?
23. Will auditors be able to effectively carry out their responsibility to evaluate the effectiveness of the audit committee's oversight?
24. If the auditor concludes that ineffective audit committee oversight is a material weakness, rather than require the auditor to issue an adverse opinion with regard to the effectiveness of the internal control over financial reporting, should the standard require that auditor to withdraw from the audit engagement?

Response to Questions 22, 23, 24:
No, it is not appropriate for the auditor to evaluate the effectiveness of the audit committee in any formalized manner. The auditor is hired, retained, fired, and the fees approved by the audit committee. Directly evaluating the hand that feeds you results in an inherent conflict of interest that is unacceptable. Of course, if the auditor determines that there are opportunities for the audit committee to improve or enhance their practices and/or processes based on their interactions with the company or the committee, the auditor has a professional responsibility to share those conclusions appropriately (with management, the audit committee, and/or the board of directors). However, mandating and formalizing such review, creates a conflict of interest that is not much different than the perceived (and actual?) conflicts the "independence" rules are trying to eradicate. A more practical conclusion may be to expect that the board's governance committee (or in the absence of such a committee, the full board) conduct/lead this evaluation. The governance committee of the board is part of the NYSE governance rules that will become effective in 2004.

If the Board does not reconsider this position (auditor evaluation of the audit committee), then question 24 comes into play. Although the audit committee has a significant role in setting the tone at the top of an organization, the management of the company has an even larger and more pervasive role in establishing and maintaining that tone. Although an ineffective audit committee might certainly result in a concern, that concern needs to be evaluated considering the situation in its entirety. If management has established and maintained an effective system of controls over financial reporting, yet the audit committee is deemed as "ineffective," that should not necessarily result in a material weakness. **Unless,** however, the ineffectiveness is considered to potentially result in more than a remote likelihood that a material misstatement would not be prevented or detected.

28. Should the Board provide specific guidance on independence and internal control-related non-audit services in the context of this proposed standard?
29. Are there any specific internal control-related non-audit services the auditor should be prohibited from providing to an audit client?

Response to Questions 28, 29:
Although there may very well be opportunities to further study and refine the prohibitions on non-audit services that may impair or impede independence of the auditor, we would suggest allowing some time for the existing standards to settle-in before revisiting this topic.

If you have any questions or would like to discuss the comments provided above, I can be reached by telephone at (402) 827-2538 or by e-mail at HalGaryn@CommercialFed.com.

Regards,

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