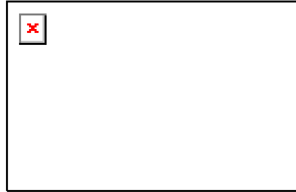
From: John Dearie [mailto:John.Dearie@financialservicesforum.org]
Sent: Monday, February 26, 2007 5:12 PM
To: Comments
Subject: Comment Re: Proposed Auditing Standard - An Audit of Internal Control Over Financial Reporting that is Integrated with an Audit of Financial Statements



February 26, 2007

Public Company Accounting Oversight Board
Attention: Office of the Secretary
1666 K Street, NW
Washington, DC 20006-2803

Re: Proposed Auditing Standard – An Audit of Internal Control Over Financial Reporting that is Integrated with an Audit of Financial Statements

This letter is submitted on behalf of the Financial Services Forum, a financial and economic policy organization comprising the chief executive officers of 21 of the largest and most diversified financial institutions with operations in the United States. The Forum works to promote policies that enhance savings and investment in the U.S. and that ensure an open, competitive, and sound global financial services marketplace. As a group, the Forum's member institutions employ more than 2 million people in 175 countries and hold combined assets of more than $16 trillion.

Please note that while we submit this letter on behalf of the Forum, the views expressed herein should not be taken to necessarily represent the specific positions of each institution comprising the Forum's membership, nor does this letter supplant other more specific comments that might be separately provided by the Forum's member institutions.

With this letter the Forum wishes to convey several important points: 1) our strong support for the enactment of the Sarbanes-Oxley Act of 2002; 2) the need for regulatory recalibration of certain aspects of the Act's implementation – particularly regarding internal controls for financial reporting, or Section 404; and, 3) the Forum's support for the new guidance proposed by the Public Company Accounting Oversight Board ("PCAOB"or "the Board") last December.

The foundation of any competitive capital market is investor confidence. When investors put their capital at risk by purchasing shares in a company or its debt securities, they must have faith that the company is telling the truth about its business and its finances. They must be sure that the company's financial statements have been prepared using high-quality accounting standards designed to accurately reflect the company's financial condition. If investors don't have that faith – or if their faith is undermined – investors will insist on a risk premium on their investment. The net effect of this "uncertainty" or "anxiety" premium is to raise the cost of capital, with clearly negative implications for business investment, risk-taking, innovation, productivity, and, therefore, job creation.

This scenario is of particular concern at a time when more than half of U.S. households own equities, and when investment decisions regarding the deployment of retirement funds are increasingly being delegated to individual beneficiaries. The number of American shareholders has risen from 30 million in 1980 to more than 84 million in 2002. And those individual investors – putting money into 401(k) pensions, mutual funds, and brokerage accounts – account for up to 80 percent of the new money flowing into U.S. stock markets.

Since the 1930s, the United States has required some of the most extensive financial disclosures, backed by one of the most robust enforcement regimes in the world. Such requirements entail substantial costs, particularly for foreign firms who must reconcile their financial statements to U.S. standards. But such costs are more than offset by the reduced cost of capital, the prestige, and other benefits that come with listing in the United States.

Unfortunately, in the boom years of the late 1990s too many forgot the critical importance of maintaining the confidence and trust of investors. As the dot-com bubble burst, a parade of corporate scandals began. Enron, WorldCom, Adelphia, Health South, Tyco, Global Crossing, Cedant, and others were accused of managerial fraud, accounting irregularities, and other governance abuses. While the vast majority of corporate officers are honest people who discharge their responsibilities with the highest ethical standards, it became apparent that some were employing questionable accounting practices and too often ethical corners were being cut.

The unfortunate effect of these scandals was to undermine investors' faith in the integrity and basic fairness of the world's greatest capital market. The subsequent drop in equity prices and the reluctance of investors to return to the markets once prices stabilized led to the loss of more than $7 trillion of equity value – nearly half of the markets' total capitalization.

The government's response came in 2002 when Congress passed and President Bush signed into law the Sarbanes-Oxley Act – the most significant piece of securities legislation passed since the Securities Acts of 1933 and 1934, the latter of which created the Securities and Exchange Commission. Sarbanes-Oxley created the PCAOB to oversee the audit profession, and created new rules to protect auditor independence. It addressed conflicts of interest faced by securities analysts, increased the penalties for financial fraud, and gave the SEC additional resources. The Act also instituted other

important safeguards, such as requiring the chief executive and chief financial officers of issuing companies to personally certify the company's financial statements, and mandated that auditors certify the adequacy of the issuer's internal controls – the so-called Section 404 provision of the statute.

In assessing the effect of Sarbanes-Oxley, it must be acknowledge that since its passage investors – including millions of individual investors – have returned to the markets, pushing the major indices to multi-year highs and creating more than $5 trillion in additional equity value.

At the same time, other developments have established a worrisome pattern:

- In 2005, the United States accounted for 20 percent of worldwide IPO proceeds, down from 35 percent in 2001.
- In 2005, 23 of the 25 largest IPOs did not list in the United States.
- In 2000, nine out of every 10 dollars raised by foreign companies through new stock offerings were raised in the United States. In 2005, the reverse was true – nine out of every 10 dollars raised by foreign companies through new company listings occurred outside the Unites States, principally in Europe.
- A recent London Stock Exchange survey of 80 international companies that went public on its market found that of those that contemplated a U.S. listing, 90 percent decided that Sarbanes-Oxley made London more attractive.

Implementation of Sarbanes-Oxley is not uniquely responsible for this troubling trend. But given the evidence, it seems clear that, in addition to the acknowledged benefits of the Act, unintended consequences have undermined the attractiveness of the U.S. capital markets for many companies – both foreign and domestic.

It is entirely in keeping with the principles of our corporate governance standards to re-evaluate whether the rules and regulations written to implement those principles are effective and appropriate:

- Do the rules and regulations achieve the intended objectives?
- Do they impose an unnecessarily high or costly burden on regulated firms, particularly smaller businesses?
- Do the costs of meeting the requirements outstrip the acknowledged benefits of listing in the U.S. markets?
- Are there steps that can be taken to alleviate some of the burden and costs without undermining investor confidence?

These are reasonable, prudent questions to ask. And preserving a strong and vital capital market is too important to the future of the United States not to ask them.

For these important reasons, the Forum applauds the new guidance proposed by the Board on December 19, 2006. In issuing the new guidance, we believe that the Board has acted properly and within its statutorily defined authority. By clarifying regulatory notions of materiality, making implementation of Sarbanes-Oxley more top-down, risk-based, and scalable for smaller companies, and removing the requirement that auditors evaluate management's assessment process, the new guidance will focus auditors' attention, energy, and resources on those aspects of a company that pose the greatest risk of material error or fraud. These ideas will form the basis of a new accounting standard that will better serve the interests of investors, both large and small, and help achieve a more appropriate balance between the disclosure- and transparency-enhancing aspects of Sarbanes-Oxley and the priority of minimizing regulatory burden and compliance costs.

The Financial Services Forum appreciates the opportunity to submit this comment letter and looks forward to working with the Board and its staff to ensure the highest standards of corporate disclosure and accountability while keeping the United States the world's capital market of choice.

Donald L. Evans
Chief Executive Officer

Rob Nichols
President and Chief Operating Officer

cc: Mark W. Olson, Chairman
Kayla J. Gillan, Member
Daniel L. Goelzer, Member
Bill Gradison, Member
Charles D. Niemeier, Member