

Sappi Ltd Group response to PCAOB

Proposed Auditing Standard – an Audit of Internal Controls Over Financial Reporting That is Integrated with an Audit of Financial Statements and related Other Proposals

Questions

A. Focusing the Audit on the Matters Most Important to Internal Control

1. Directing the Auditor's Attention Towards the Most Important Controls

1. Does the proposed standard clearly describe how to use a top-down approach to auditing internal control?

In our opinion this is only partly achieved. Where the previous guidance was fairly prescriptive about the way in which significant locations are identified first the current guidance provides significant latitude in determining which locations should be visited. We appreciate that this latitude is an inevitable consequence of a risk based approach and will never result in a 'clear description' as to how it should be applied.

2. Does the proposed standard place appropriate emphasis on the importance of identifying and testing controls designed to prevent or detect fraud?

Yes

3. Will the top-down approach better focus the auditor's attention on the most important controls?

Yes. Notwithstanding our comments in one above, we believe that a top-down approach will better focus attention on the most important controls.

4. Does the proposed standard adequately articulate the appropriate consideration of company-level controls and their effect on the auditor's work, including adequate description of when the testing of other controls can be reduced or eliminated?

Yes

2. Emphasizing the Importance of Risk Assessment

5. Does the proposed standard appropriately incorporate risk assessment, including in the description of the relationship between the level of risk and the necessary evidence?

Yes. For 'super key' (our terminology) controls - covering high risk areas - full evidence is required. For lower risk areas - prior year evidence plus roll forward type procedures are possible / walkthrough testing evidence suitable. Rotational testing not yet allowed. This is unfortunate and we would support this further change.

6. Would the performance of a walkthrough be sufficient to test the design and operating effectiveness of some lower risk controls?

Yes - especially suitable for Sappi SOX controls many of which only require a small sample to be tested. For applicable controls the evidence will essentially be the same

as if we were testing the control - so the impact on "use of others work" should be minimal).

3. Revising the Definitions of Significant Deficiency and Material Weakness

7. Is the proposed definition of "significant" sufficiently descriptive to be applied in practice? Does it appropriately describe the kinds of potential misstatements that should lead the auditor to conclude that a control deficiency is a significant deficiency?

Yes

8. Are auditors appropriately identifying material weaknesses in the absence of an actual material misstatement, whether identified by management or the auditor? How could the proposed standard on auditing internal control further encourage auditors to appropriately identify material weaknesses when an actual material misstatement has not occurred?

Yes

9. Will the proposed changes to the definitions reduce the amount of effort devoted to identifying and analyzing deficiencies that do not present a reasonable possibility of material misstatement to the financial statements?

Yes. Too much emphasis was placed on the aggregation of low-level deficiencies with the previous guidance (as prepared by the 9 audit firms).

4. Revising the Strong Indicators of a Material Weakness

10. Should the standard allow an auditor to conclude that no deficiency exists when one of the strong indicators is present? Will this change improve practice by allowing the use of greater judgment? Will this change lead to inconsistency in the evaluation of deficiencies?

Yes. While this does place a greater emphasis on audit judgment there are a number of circumstances that can be contemplated where a strong indicator should not automatically lead to conclusions about deficiencies.

6. Clarifying the Role of Interim Materiality in the Audit

11. Are further clarifications to the scope of the audit of internal control needed to avoid unnecessary testing?

No

12. Should the reference to interim financial statements be removed from the definitions of significant deficiency and material weakness? If so, what would be the effect on the scope of the audit?

Yes. We do not believe that the removal should have an impact on the scope of the audit.

B. Eliminating Unnecessary Procedures

1. Removing the Requirement to Evaluate Management's Process

13. Will removing the requirement for an evaluation of management's process eliminate unnecessary audit work?

Yes.

14. Can the auditor perform an effective audit of internal control without performing an evaluation of the quality of management's process?

Yes. Management's processes are part of the overall system of internal control. Auditors will still have access to control descriptions, evaluations and process flow documentation. Reviewing this documentation will facilitate their conclusion although they do not have to review the process in itself.

15. Will an opinion only on the effectiveness of internal control, and not on management's assessment, more clearly communicate the scope and results of the auditor's work?

Yes.

2. Permitting Consideration of Knowledge Obtained During Previous Audits

16. Does the proposed standard appropriately incorporate the value of cumulative knowledge?

Almost. We are of the opinion that a well considered system of rotational testing is risk based in itself and would have led to further efficiencies.

17. What are the circumstances in which it would be appropriate for the auditor to rely upon the walkthrough procedures as sufficient evidence of operating effectiveness?

There should have been no material changes in people or processes and very few is any significant findings during the previous year's testing. Management's own testing plans might provide further assurance enabling this approach to be taken.

3. Refocusing the Multi-location Testing Requirements on Risk Rather than Coverage

18. Will the proposed standard's approach for determining the scope of testing in a multi-location engagement result in more efficient multi-location audits?

Yes. We believe that this is one of the most important aspects of the changed guidance although it might have been useful to supplement with a degree of rotational testing. It is also not always practical to perform a detailed risk assessment and identify major classes of transactions at a central level. Quantitative evaluations are inherently easier. Notwithstanding the challenge, we believe that the changed guidance is appropriate

4. Removing Barriers to Using the Work of Others

19. Is the proposed standard's single framework for using the work of others appropriate for both an integrated audit and an audit of only financial statements? If different

frameworks are necessary, how should the Board minimize the barriers to integration that might result?

Yes

20. Does the proposed definition of relevant activities adequately capture the correct scope of activities, including activities that are part of the monitoring component of internal control frameworks?

No

21. Will requiring the auditor to understand whether relevant activities performed by others identified control deficiencies, fraud, or financial statement misstatements improve audit quality?

Yes

22. Is the principal evidence provision that was in AS No. 2 necessary to adequately address the auditor's responsibilities to obtain sufficient evidence?

Yes

23. Does the proposed standard provide an appropriate framework for evaluating the competence and objectivity of the persons performing the testing? Will this framework be sufficient to protect against inappropriate use of the work of others? Will it be too restrictive?

Yes

24. Has the Board identified the right factors for assessing competence and objectivity? Are there other factors the auditor should consider?

Yes

25. What will be the practical effect of including, as a factor of objectivity, a company's policies addressing compensation arrangements for individuals performing the testing?

Weren't sure what was meant here

5. Recalibrating the Walkthrough Requirements

26. Will requiring a walkthrough only for all significant processes reduce the number and detail of the walkthroughs performed without impairing audit quality?

Yes

27. Is it appropriate for the auditor to use others as direct assistance in performing walkthroughs? Should the proposed standard allow the auditor to more broadly use the work of others in performing walkthroughs?

Yes

C. Scaling the Audit for Smaller Companies

28. Does the proposed standard on auditing internal control appropriately describe how auditors should scale the audit for the size and complexity of the company?

29. Are there other attributes of smaller, less-complex companies that the auditor should consider when planning or performing the audit?

30. Are there other differences related to internal control at smaller, less complex companies that the Board should include in the discussion of scaling the audit?

31. Does the discussion of complexity within the section on scalability inappropriately limit the application of the scalability provisions in the proposed standard?

32. Are the market capitalization and revenue thresholds described in the proposed standard meaningful measures of the size of a company for purposes of planning and performing an audit of internal control?

D. Simplifying the Requirements

III. Proposed Rule 3525 – Audit Committee Pre-approval of Services Related to Internal control

33. Is there other information the auditor should provide the audit committee that would be useful in its pre-approval process for internal control-related services?

VI. Effective Date

34. How can the Board structure the effective date so as to best minimize disruption to on-going audits, but make the greater flexibility in the proposed standards available as early as possible? What factors should the Board consider in making this decision?

The Board should permit auditors to apply the guidance with immediate effect for the following reasons:

- *Represents the boards current thinking*
- *Failure to do so allows for continued audit inefficiencies in certain areas.*
- *We have worked with our auditors to identify areas where their testing can be reduced assuming that the guidance remains in its current form. In this way the disruption should be limited.*