February 26, 2007

Public Company Accounting Oversight Board
Attention: Office of the Secretary
1666 K Street N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 21 - Proposed Auditing Standard – *An Audit of Internal Control Over Financial Reporting That Is Integrated With An Audit of Financial Statements; And Related Other Proposals*

Dear Mr. Secretary:

Veris Consulting, LLC ("Veris") is pleased to respond to the request for comment from the Public Company Accounting Oversight Board ("PCAOB" or the "Board") on the proposed auditing standard, *An Audit of Internal Control Over Financial Reporting That Is Integrated With An Audit of Financial Statements* (the "proposed standard") and related other proposals. We set forth below our comments for consideration by the Board as it deliberates regarding a final standard on this subject. Our comments are intended to assist the Board in its efforts to enhance the quality of financial reporting by public companies and the quality of audit with respect to such financial reporting with the overall objective of restoring confidence in our capital markets system.

Our comments have been organized into two main sections: 1) Executive Summary – which includes a detailed analysis of our basic difference with the Board's approach in the proposed standard; and 2) General Section – which covers our response to the specific questions posed by the PCAOB in its release.

We would be pleased to discuss our comments with you or other members of the Board. If you have any questions, please contact Noeleen Doelger, Managing Director, or Vishal Mehta, Director, at (732) 747-9800.

Very truly yours,

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I. <u>Executive Summary</u>

We would like the Board to consider our comments in light of their and the SEC's stated objective of reducing the cost of compliance with the Sarbanes-Oxley Act's requirements, while enhancing the quality of the audit of the financial statements of public companies.

Given the above objective, we concur with and endorse the Board's proposal to eliminate the auditor's opinion on management's process for reporting on internal controls over financial reporting ("ICFR"). However, we fundamentally disagree with the Board's dichotomy between the test of controls in an audit of financial statements and the test in an audit of internal control, as it defeats the purpose of integrating the "two" audits. In fact, we believe that there should be a single audit with dual objectives – 1) opining on the internal controls and 2) opining on the financial statements.

Therefore, we recommend to the Board that they should consider revising Appendix B – Integration of Audits (pages B1 – B11) of the proposed standard and clearly state that, while performing an ***audit of financial statements and ICFR***, the auditor ***must*** adopt a wholly compliance-based approach -

i. Requiring the performance of substantive tests for financial statement assertions that are deemed insignificant or in the case of controls which the auditor evaluates as deficient; and
ii. Considering the results of his/her test of controls to alter the nature, extent and timing of substantive procedures, otherwise.

We believe this approach will truly integrate the audit process and significantly reduce the cost by ensuring the use of or directing auditors to use a single audit team to conduct a risk-based audit. Please refer to the flow chart in the attached Appendix for additional clarification.

We do recognize that the above mentioned approach would require a change in the auditor's mindset since, under traditional auditing standards, performing a wholly substantive audit has always been a valid option. In addition, the Board would need to revise the language of the proposed standard to delete any references to the separate audits, as well as to emphasize the importance of the link between materiality, significant account balances, financial statement assertions and control risk as the drivers of audit efficiency.

Some of the other areas that the Board would also need to reassess in the proposed standard are as follows:

- Broaden the scope of the proposed standard to include and address multiple control frameworks, given the SEC's guidance to management that it may select any control framework, other than COSO, for purpose of its assertion regarding internal controls.

- Timing of testing of information technology ("IT") controls directly related to financial reporting, since the pervasive and evolving nature of these controls affects the accuracy of financial statements on a continuous basis during the year.

II. <u>General Section</u>

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

1. Directing the auditor's attention towards the most important controls

We believe that the Board has adequately described the "top down approach" as well as the intended benefit of using this approach on the audit. However, the Board should consider reorganizing the paragraphs to mirror the logical sequence of tasks followed while applying the top-down approach. That is, paragraphs 24 to 29 under "*Identifying Significant Accounts*"; paragraphs 30 and 31 under "*Identifying Relevant Assertions*" and paragraphs 32 through 40 under "*Identifying Major Classes of Transactions and Significant Processes (including performing walkthroughs)*" should precede paragraphs 17 through 23 under *Identifying Company-Level Controls*.

The rationale for this reorganization is that, while applying the top-down approach, an auditor first determines the significant account balances ("SAB") and then the relevant financial statement assertions applicable for each significant account balance, followed by identifying the major classes of transactions ("MCOT") and significant processes. In other words, the identification of company-level controls important to an auditor's conclusion, without identification of significant account balances, appears to be counterintuitive.

Further, we believe that the Board should consider enhancing the guidance relating to fraud. Since fraud risk is present both at the entity-level (e.g., management override) and at account balance level (e.g., cash, accruals, write-offs, etc.), the Board should clarify that fraud risk should be a required criterion during the auditor's risk assessment process as well as during the identification of important internal controls to test.

2. Emphasizing the importance of risk assessment

Please refer to our suggested comments in the Executive Summary section above. In addition, we believe that performance of a walkthrough would be a sufficient test of the design and operating effectiveness of a low risk control and recommend that the proposed standard reflect this.

3. Revising the definitions of Significant Deficiency and Material Weakness

The Board's current proposals to:

- replace "more than remote likelihood" with "reasonably possible" and "more than inconsequential" with "significant"; and
- define material weaknesses more narrowly to exclude an aggregation of significant deficiencies

will simplify the auditor's evaluation of control deficiencies, but only to a limited extent. We strongly believe that the PCAOB should consider enhancing the guidance in paragraphs 74 and 75 to include language that requires the auditor to assess the magnitude of a potential misstatement based on the materiality threshold established for the audit of the financial statements. This linkage will further promote the Board's (and the SEC's) underlying objective of integrating the audit of internal control and financial statement audit (See questions 8 and 9 on page 11 of the PCAOB Release 2006-007).

4. Revising the strong indicators of a Material Weakness

We concur with the Board's proposal and believe that the proposed standard should allow an auditor to conclude whether a deficiency exists or not when one of the strong indicators is present based on enhanced testing and use of judgment, rather than automatically conclude that a deficiency exists.

5. Clarifying the role of materiality in the audit

We believe that further clarifications to the scope of the audit are not necessary. In addition, the reference to interim financial statements should be retained in the definition of significant deficiency and material weakness. ***However***, as stated in section 3. above, even though the Board has clarified that auditors should use only one materiality threshold, it should consider providing further guidance to auditors on how to apply the concept of materiality to evaluation of risk (scoping) and measuring control deficiencies (opinion).

6. Clarifying the role of interim materiality in the audit

Please refer to our comment in section 5 above.

B. Eliminating Unnecessary Procedures

1. Removing the requirement to evaluate management's process

Please refer to our comments in the Executive Summary section above.

2. Permitting consideration of knowledge obtained during previous audits

The proposed standard appropriately incorporates the value of knowledge obtained by the auditor in prior year audits, such that it should only affect the auditor's assessment of risk related to a specific account balance and his/her determination of the nature, timing and extent of test of controls in a subsequent year audit.

Further, with specific reference to Question 17 on page 20, we believe that a walkthrough would normally be sufficient evidence of operating effectiveness for controls that have been assessed as low risk.

3. Refocusing the multi-location testing requirement on risk rather than coverage

While the Board's intention is to limit testing to only those locations which present a reasonable or higher possibility of a material misstatement in the entity's consolidated financial statement, we believe that the proposed standard should include specific language indicating that this assessment of risk of misstatement should be made at the account balance level. This will prevent situations where the auditor (and company management) may exclude a location on the basis that its net result of operations is immaterial (in light of the consolidated entity's net income/loss), in spite of the fact that such location may have revenue or expense account balances which include one or more balances that present a high probability of risk of material misstatement.

4. Removing barriers to using the work of others

We concur with the Board's views on proposing a single standard framework for using the work of others (proposed standard to replace SAS 65). We also believe that the removal of the "principal evidence" clause will reduce the overall audit effort and that the proposed standard adequately and appropriately captures the scope of activities and an auditor's responsibilities, as well as the factors for evaluating the competency and objectivity of "others" etc.

5. Recalibrating the walkthrough requirements

We partly agree with the Board's proposed changes to the walkthrough requirements. While the proposal to perform walkthroughs at a process level will lead to efficiencies, it should be further clarified in the proposed standard that often there will be circumstances that would merit performing a walkthrough at a ***major class of transaction*** level. For instance, if an insurance filer's revenues are comprised of multiple lines of property and casualty business, and each line of business is equally material/significant to the financial statements, the auditor should perform the walkthrough for each line of business (***i.e. MCOT***) and not at the overall revenue process level.

However, we disagree with the second proposal, and strongly believe that the auditor (or audit staff) must perform all walkthroughs himself/herself as the primary objective of the walkthrough is to obtain an understanding of the process "end-to-end" and that objective should not be delegated. In addition, given that the SEC has allowed management some flexibility in the nature and extent of documentation that should be maintained on processes and ICFR, the auditor's walkthrough assumes even more significance as it eliminates any reliance on potentially deficient documentation.

C. Scaling the Audit for Smaller Companies

We are in general agreement with the Board's proposed guidance on the audit of small companies. However, we believe the potential to scale the audit should be based on complexity, rather than "size and complexity" as it currently reads. Therefore, scaling the audit would be applicable to all filers, not just small companies. The following are suggestions for enhancements for the Board's consideration:

Company level controls

Most small companies have a relatively flat organizational structure and, consequently, an extensive involvement by senior management in day-to-day control activities, as well as period/year end financial close activities. Given this reality, we believe that the Board's statement in the last sentence of the second bullet of paragraph 12 (page A1-9 of the proposed standard) is prone to subjectivity and susceptible to misuse. Hence, we recommend that the Board provide examples of "alternative controls" for situations where an auditor establishes that management is extensively involved in performing key control activities. In such cases, the auditor should expand his test of controls beyond the test of company-level controls to test such additional controls so as to mitigate the risk of management override or lack of segregation of duties.

Evaluating IT controls

The small business IT control discussion (page A1-12 of the proposed standard) should be expanded to highlight differences between small companies that use prepackaged software and those that rely on home-grown or proprietary systems.

Proprietary systems offer more challenges as the auditor needs to understand risks, such as programmer access to production systems and change controls. In addition, system development lifecycle controls must be assessed. Issues such as ensuring management buy-in for the source code changes, QA testing, integration testing and edit checking should all be considered as part of the overall risk assessment process. These types of risks directly impact the accuracy and completeness of financial data processed on an ongoing basis by the entity's financial reporting system.

Further, prepackaged software rarely facilitates all aspects of financial reporting for a small company. Finance departments often generate several end-user controlled and developed desktop applications (i.e., spreadsheets) that are either fed by source systems or feed source systems. These “desktop” end-user owned applications form the crux of general IT control confusion when small companies attempt to comply with Sarbanes-Oxley requirements for IT controls. Desktop applications are inherently weak in terms of supporting Sarbanes-Oxley related change and security controls. In order to comply with Sarbanes-Oxley, smaller companies are required to create burdensome assessment matrices that depend on an unclear and sometimes arbitrarily defined combination of human and IT controls in order to prevent or detect potential flaws in the logical processing of data within the application. This “gray area” between IT and financial process controls needs to more clearly defined so that companies can adopt standardized approaches to documentation and testing. Ideally, a move from reliance on desktop applications to a more robust and centralized solution maintained by IT should be encouraged by the Sarbanes-Oxley compliance community to alleviate this issue.

In addition, IT controls should be evaluated on a quarterly basis as the systems being evaluated are typically more dynamic and subject to change as compared to the business processes they support. Often systems are implemented or decommissioned within an accounting period or cycle. To address this issue, the auditor should ensure that documented risks, controls and tests support the relevant systems during the relevant time frames.

Proposed Rule 3525 – Audit Committee Pre-approval of Services Related to Internal Control

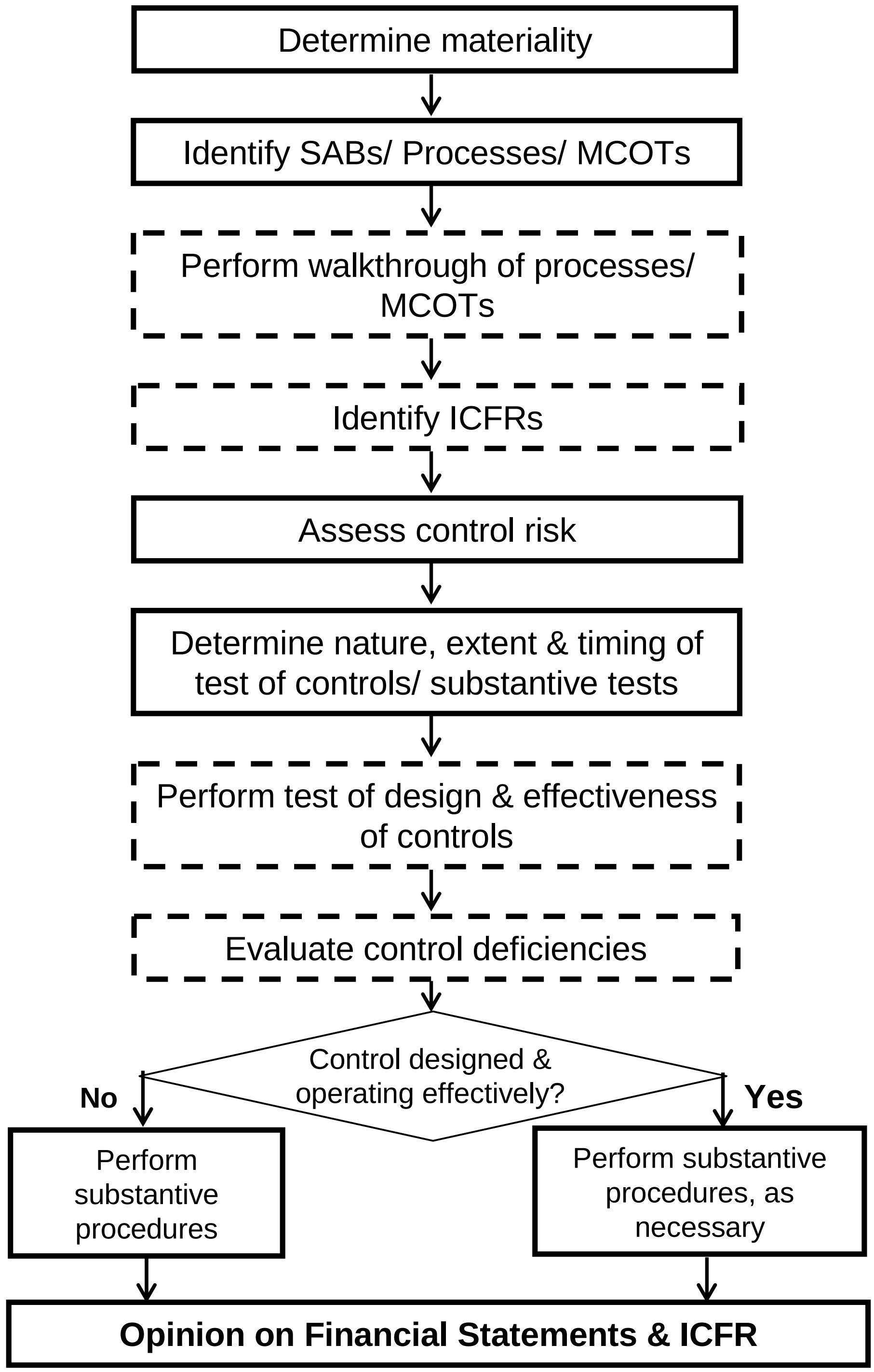
We concur with the Board’s proposed Rule and have no additional comments or amendments.

Effective Date

In order to determine the effective date of the proposed standard, we recommend that the Board consider that the revised guidance will impact not only the auditor’s approach, but also management’s process for making the assertion. Hence, it is important to make the final guidance available in time for both filers and registered public accounting firms. In addition, given that the Board’s objective of issuing the proposed standard is congruent with the SEC’s goal of providing guidance to filers on how to make the assertion process cost effective, it is important the Board deliberates and gives due consideration to all comments received.

APPENDIX

Flow Diagram for Integrated Audit of Financial Statements and ICFR



Note 1: Activities within dotted lines represent activities that are optional or not applicable in an audit of financial statements
Note 2: In a traditional audit of financial statements, the auditor may perform wholly substantive procedures even if he/she assesses a control as effective