

August 15, 2008

Larry E. Rittenberg, Chair
Committee of Sponsoring Organizations of the Treadway Commission

Re: Comments on Exposure Draft of *Guidance on Monitoring Internal Control Systems*

Dr. Rittenberg and the COSO Board:

The American Institute of Certified Public Accountants (AICPA) respectfully submits the following comments on the Committee of Sponsoring Organizations of the Treadway Commission (COSO) exposure draft of the document *Guidance on Monitoring of Internal Control Systems*.

The comments herein reflect the feedback from the AICPA Business and Industry Executive Committee (BIEC) and the Technical Issues Committee (TIC) of the Private Companies Practice Section of the AICPA. The BIEC represents the approximately 138,000 AICPA members who are employed by businesses in a wide variety of roles in a broad range of industries. TIC represents the views of local and regional CPA firms with private company clients in the technical accounting and auditing standards-setting arena.

We commend the leadership of COSO in developing this Guidance, and appreciate the opportunity to comment on behalf of our members in business and industry and our members in local and regional CPA firms serving private company clients. Please note that the views of the public company audit profession are not addressed in this letter – the public company audit perspective will be addressed in a separate letter being submitted by the Center for Audit Quality. The Center for Audit Quality is an autonomous public policy organization serving investors, public company auditors and the capital markets and is affiliated with the AICPA.

Comments

Both the members of BIEC and TIC found the Exposure Draft of the Guidance to be very well done and responsive to comments provided on the preliminary draft circulated in September 2007.

The document is comprehensive and goes into sufficient detail to provide much needed clarity on a number of concepts that are important to companies designing and implementing internal control systems and the monitoring components essential to their continued effective functioning.

In particular:

- The characteristics of evaluators and the continuum of objectivity is a useful construct and the discussion addressing both the limitations and value of self-review is on point.
- The section emphasizing the importance of knowing when internal controls have changed, or need to change, is very well written and critical to maintenance of effective controls.
- The addition of the discussion about the importance of monitoring controls outsourced to others addresses an important vulnerability for smaller companies, especially in the pension area.
- The section in Volume II providing guidance on IT controls is clear and concise and the example in Volume III as it relates to IT controls is also very helpful.
- The discussions on costs/benefits and scalability should also prove to be very useful, although it should be noted that the Guidance will be challenging to implement for companies at the smaller end of the size spectrum.
- The revenue recognition example that was used in Volume II is particularly helpful, as are the additional examples provided in Volume III.

Two specific recommendations for the Guidance follow:

1. Paragraph seven specifically addresses the identification and correction of control deficiencies. This is arguably the primary purpose of monitoring, but is not included in either paragraph three (reasons for developing guidance) or paragraph six (value to the organization). Inclusion of the identification and correction of control deficiencies in paragraph six as a primary benefit to the organization would more clearly articulate the purpose and value of monitoring.
2. In reviewing the Glossary at the end of Volume II, TIC noted that the definition of a control deficiency is not consistent with the definition included in PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, or the expected definition in the exposed revision to SAS 112 (AU Section 325), *Communicating Internal Control Related Matters Identified in an Audit*. Conforming this definition should be considered to mitigate potential confusion.

In Conclusion

We think that this document meets the objectives identified by COSO to 1) help organizations improve the effectiveness and efficiency of their internal control systems and 2) provide practical guidance that illustrates how monitoring can be incorporated into an organization's internal control processes.

On behalf of the AICPA and the members of the Business and Industry Executive Committee and Technical Issues Committee that contributed to the drafting of this letter, thank you for the opportunity to comment on this exposure draft.

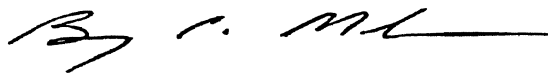
AICPA Comments – COSO *Guidance on Monitoring Internal Control Systems*

If you have any questions regarding the comments in this letter, please contact Chris McKittrick at 919-402-4085 or CMckittrick@aicpa.org.

Respectfully submitted on behalf of the AICPA Business and Industry Executive Committee and Technical Issues Committee,



Patricia Cochran, CPA
Chief Financial Officer,
Vision Service Plan
Rancho Cordova, CA
Chair, AICPA Business and Industry Executive Committee



Barry C. Melancon, CPA
President and CEO
AICPA

COSO Guidance on Monitoring Internal Control Systems
Public Comment Form – Spring 2008

Thank you in advance for providing feedback on COSO's exposure draft, *Guidance on Monitoring Internal Control Systems*. Your candid responses will allow us to gauge its effectiveness and improve the final document, benefiting organizations of all sizes and their stakeholders.

This comment form follows the order of the Guidance. You may also complete it online (which is our preferred method of collecting feedback) through a link posted at <http://www.coso.org/guidance.htm>. Each section contains brief questions regarding the Guidance and also offers respondents an opportunity to provide general feedback unrelated to the questions. If you prefer, you may provide feedback without answering the questions. The demographic information requested in the last section will help us group and analyze the responses.

You may submit this form or other written feedback via email to COSOMonitoring@gt.com or fax it to COSO Monitoring at 704.337.2979.

We would like to receive all comments by August 15, 2008. Note that they will be posted to the COSO Web site as submitted, with no redaction of identifying information.

If you have any questions about accessing or responding to the discussion document, please contact Jay Brietz at 704.632.6916.

We know your time is valuable, and we thank you again for your thoughtful completion of this comment form. Your feedback is integral to the success of the final document.

Larry E. Rittenberg, PhD, CPA, CIA
Chairman, COSO

Questions/Commentary

Volume II – The Guidance

Chapter I. Monitoring as a Component of Internal Control Systems

1. Does the Guidance adequately describe the role of internal control monitoring (paragraphs 6–10)?

Yes

Comments:

Paragraph 7 specifically addresses the identification and correction of control deficiencies. This is arguably the primary purpose of monitoring, but is not included in either par. 3 (reasons for developing guidance) or par. 6 (value to the organization). This should be incorporated as a primary benefit in par. 6. Presentation would also be improved if these benefits were numbered and presented in a hierarchical order - micro to macro view.

2. Additional comments regarding Chapter I.

Comments:

The box accompanying par. 4 introduces the two principles extracted from the original COSO Framework, including principle 19 - ongoing and/or separate evaluations, but these are not discussed in the narrative. Absent mention of ongoing and/or separate evaluations par. 7 could be construed to imply that effective monitoring must be ongoing.

Chapter II. Establishing a Foundation for Monitoring

3. Is the model for monitoring presented in paragraph 19 a complete and accurate outline of the monitoring process?

Yes

Comments:

None

4. Do you agree with the description of the roles of management and the board with respect to monitoring (see paragraphs 23–24)?

Yes

Comments:

While the board has oversight responsibility for what goes on at company (including monitoring as described here), the partnership between the board and senior-management and their shared responsibility should be emphasized.

In addition to objectivity considerations, both the management team, the board and audit committee often need different competencies or expertises to ensure proper monitoring.

The role of the audit committee and internal audit is mentioned briefly in par.22. The second paragraph of the Applying the Concepts box argues for internal audit as organizations increase in size and complexity. It might be helpful to make the point about the importance of both internal audit and audit committees in the text.

5. Do you agree with the description of the characteristics of evaluators (see paragraphs 25-33)?

Yes

Comments:

The discussion in paragraph 30 regarding self review is right on point.

6. Is the discussion about establishing a baseline understanding of internal control effectiveness clear, correct, complete, and useful (see paragraphs 34–36)?

Yes

Comments:

The discussion about the importance of knowing when internal controls have changed and how that should impact monitoring was very well written

7. Additional comments regarding Chapter II.

Comments:

None

Chapter III. Designing and Executing Monitoring Procedures

8. Figure 7 on page 18 and paragraphs 42–49 are designed to provide an overview of the core of monitoring — designing and executing monitoring procedures. Do the graphic and related summary paragraphs properly summarize the process of monitoring?

Yes

Comments:

The revenue recognition key control in the "Applying the Concepts" box was very helpful. The second bullet of par. 46 (excerpted below) is an important aspect of key controls. It might be helpful to incorporate this concept into the examples under application techniques. "Their operation might prevent other control failures or detect such failures before they have an opportunity to become material to the organization's objectives."

9. The Guidance indicates that effective and efficient monitoring evaluates controls that address “meaningful risks” to an organization’s objectives. Paragraphs 50–54 provide guidance regarding assessing risks and how prioritizing risk influences monitoring. The intent is to provide guidance (1) without being prescriptive as to how risk assessment should be done, and (2) without delving so deeply into the risk assessment component that the focus of the Guidance shifts away from monitoring. Do you believe the Guidance properly addresses the role of risk assessment in the context of internal control monitoring?

Yes

Comments:

None

10. The Guidance defines the term “key controls” (see paragraphs 46–47 and 55–57). The project team chose to define the term because (1) it is widely used in practice, but is not consistently defined; and (2) the Guidance proposes that, in order to conclude that the internal control system effectively addresses a given risk, organizations may not need to evaluate every control that addresses that risk — thus, the term distinguishes between controls that will be subjected to monitoring procedures and those that will not. Do you believe the concept of “key controls” is properly addressed in the Guidance?

Yes

Comments:

Again, clearly illustrating the two points defining key controls would be helpful. Otherwise, there are plenty of good examples, particularly the channel-stuffing one.

11. Information that is evaluated to assess controls effectiveness provides varying levels of support. The Guidance defines “persuasive information” as that which is capable of providing adequate support for a conclusion about the effectiveness of internal control. Persuasive information is further defined as that which is “suitable and sufficient in the circumstances” (see paragraphs 59–60). Do you agree with the general premise of persuasive information as outlined in the Guidance?

Yes

Comments:

None

12. The Guidance discusses the difference between direct and indirect information as being one of the primary factors influencing the persuasiveness of information. Feedback from the September public discussion document indicated broad support for this aspect of the Guidance, but also indicated a need to refine and clarify the material. Is the current discussion of direct and indirect information (in paragraphs 64–72 and in the Applying the Concepts section beginning on page 34) clear, correct, complete, and useful?

Yes

Comments:

None

13. The Guidance states that reliable information is accurate, verifiable, and from an objective source (paragraphs 73–75). Is the concept of reliability, as described in the document, clear, correct, complete, and useful?

Yes

Comments:

None

14. Is the concept of timeliness of information (paragraphs 76–77), as described in this document, clear, correct, complete, and useful?

Yes

Comments:

None

15. The “Sufficient Information” section (paragraphs 78–79) has been expanded based on feedback from the September public discussion document. Is this expanded material clear, correct, complete, and useful?

Yes

Comments:

None

16. Based on feedback from the September discussion document, the section regarding “Ongoing Monitoring and Separate Evaluations” has been simplified. It now more clearly articulates that the primary difference between the two is not how they are performed, but how often and by whom. The Guidance then addresses the factors an organization might consider in deciding between the two processes. Do you believe this section is clear, correct, complete, and useful?

Yes

Comments:

None

17. A paragraph has been added to the document to address the monitoring of controls outsourced to others (paragraph 90). Is this paragraph clear, correct, complete, and useful?

Yes

Comments:

As mentioned in our general comments, this area cannot be emphasized enough. Entities that outsource controls to others often fail to monitor what outside third parties are doing for them, especially in the pension area.

18. The “Using Technology for Monitoring” section has been simplified from the September 2007 draft, and a discussion regarding “continuous controls monitoring” has been added (see paragraphs 91–94). Is this section clear, correct, complete, and useful? (Note: Some commenters to the September 2007 discussion document indicated a desire for direction in applying the monitoring guidance to controls over information technology (IT). A comprehensive discussion regarding monitoring IT controls has been included in Volume III.)

Yes

Comments:

This section was clear and useful. Consideration should be given in Paragraph 92 to referring to the comprehensive example that is in Volume III

19. Additional comments regarding Chapter III.

Comments:

None

Chapter IV. Assessing and Reporting Results

20. Is the section “Prioritizing and Communicating Results” clear, correct, complete, and useful?

Yes

Comments:

It would be helpful in the "Applying the Concepts" Box (Volume II, page 46) for this area if some examples were given for each of the relevant risks recognizing that judgment could be different for individual readers. TIC is looking for something similar to how the examples are presented in the "Applying Concepts" Box after paragraph 58 (Volume II, pages 24-26).

21. Is the section “Reporting Internally” clear, correct, complete, and useful?

Yes

Comments:

22. Is the section “Reporting Externally” clear, correct, complete, and useful?

Yes

Comments:

The cost/ benefit information included in paragraphs 107 and 108 are very helpful.

23. Additional comments regarding Chapter IV.

Comments:

None

Chapter V. Scalability of Monitoring

24. Chapter V, “Scalability of Monitoring,” is designed to show how monitoring might differ between organizations based on their size and complexity. It is designed to complement and summarize other references to size and complexity that are spread throughout the document. Is this chapter clear, correct, complete, and useful?

Yes

Comments:

TIC did not find the "Applying the Concepts" Box to be all that helpful in this section. It appeared to be repetitive of what had already been discussed in the text of the guidance.

Section VI. Assessing the Effectiveness and Efficiency of Monitoring

25. Is Chapter VI, "Assessing the Effectiveness and Efficiency of Monitoring," clear, correct, complete, and useful?

Yes

Comments:

None

Other General Areas/Topics

26. Does the Executive Summary (Volume I) effectively summarize the guidance contained in Volume II?

Yes

Comments:

None

27. Apart from your comments above, should anything be added or changed to improve the Guidance, making it more practical to implement? If so, please summarize your recommended additions or changes below.

Yes

Comments:

Glossary-2 -- The definition of "Deficiency or internal control deficiency" is not consistent with either PCAOB Auditing Standard 5 or the ASB's proposed clarification of AU 325. The definitions should be conformed to avoid confusion.

28. Overall, do you believe the document advances the understanding of what effective monitoring should look like in any given organization?

Yes

Comments:

None

Volume III – Application Techniques

Chapters II–IV. Brief Examples Linked to Volume II Chapters

29. Chapters II–IV of Volume III contain brief examples of how various organizations currently monitor internal control in ways that are consistent with the concepts embodied in Volume II — the Guidance and are organized to correspond with the Guidance. As the introduction to Volume III indicates, the examples are not intended to mandate how monitoring should be performed, but to articulate how the Guidance might be applied. Do the examples achieve that objective? (Note: Please elaborate if you believe certain of the examples should be edited or deleted or if you recommend inclusion of other examples.)

Yes

Comments:

30. The appendices to Volume III relate to the examples discussed in question #29 and show some of the tools the various organizations use for monitoring. Are the appendices helpful without appearing to be prescriptive?

Yes

Comments:

Chapter V. Comprehensive Examples

31. Chapter V of Volume III contains comprehensive examples of how two organizations monitor internal control over a given risk area. These examples attempt to demonstrate application of the monitoring process from start to finish, as outlined in the Guidance. Like the earlier examples, those in Chapter V are intended to be descriptive rather than prescriptive. Do these two examples help demonstrate application of the Guidance?

Yes

Comments:

32. Chapter V of Volume III also contains a discussion of monitoring information technology (IT) controls that address financial reporting-related risks. This discussion was included because (1) many people have requested specific guidance regarding monitoring IT controls related to financial reporting, (2) IT-related risks are pervasive across most organizations, and (3) the ways in which those risks are controlled are fairly consistent across organizations, making the discussion applicable in a broad sense. Without being prescriptive, does the discussion about monitoring IT controls articulate how such monitoring might be performed?

Yes

Comments:

33. Additional comments regarding Volume III.

Comments:

Demographic Information ---

34. Your name

AICPA Business and Industry Executive Committee & PCPS Technical Issues Committee

35. Your email address

kwitt@aicpa.org

36. Your position (select the position from which you answered the questions above)

[Click Here to Select Position](#)

Member committees of professional association

37. Country

USA

38. Name of organization (should correspond to position selected in Question 36 above)

AICPA

39. Classification of the above-named organization (select one)

Professional association

40. Annual revenues of the above-named organization

[Click Here to Select Revenue Category](#)

41. Public float (market cap) of the above-named organization, if a public company

[Click Here to Select Public Float Category](#)