

Update on Revisions to the COSO Framework for Internal Controls

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COMPLIANCE WEEK 2012

Internal Control-Integrated Framework

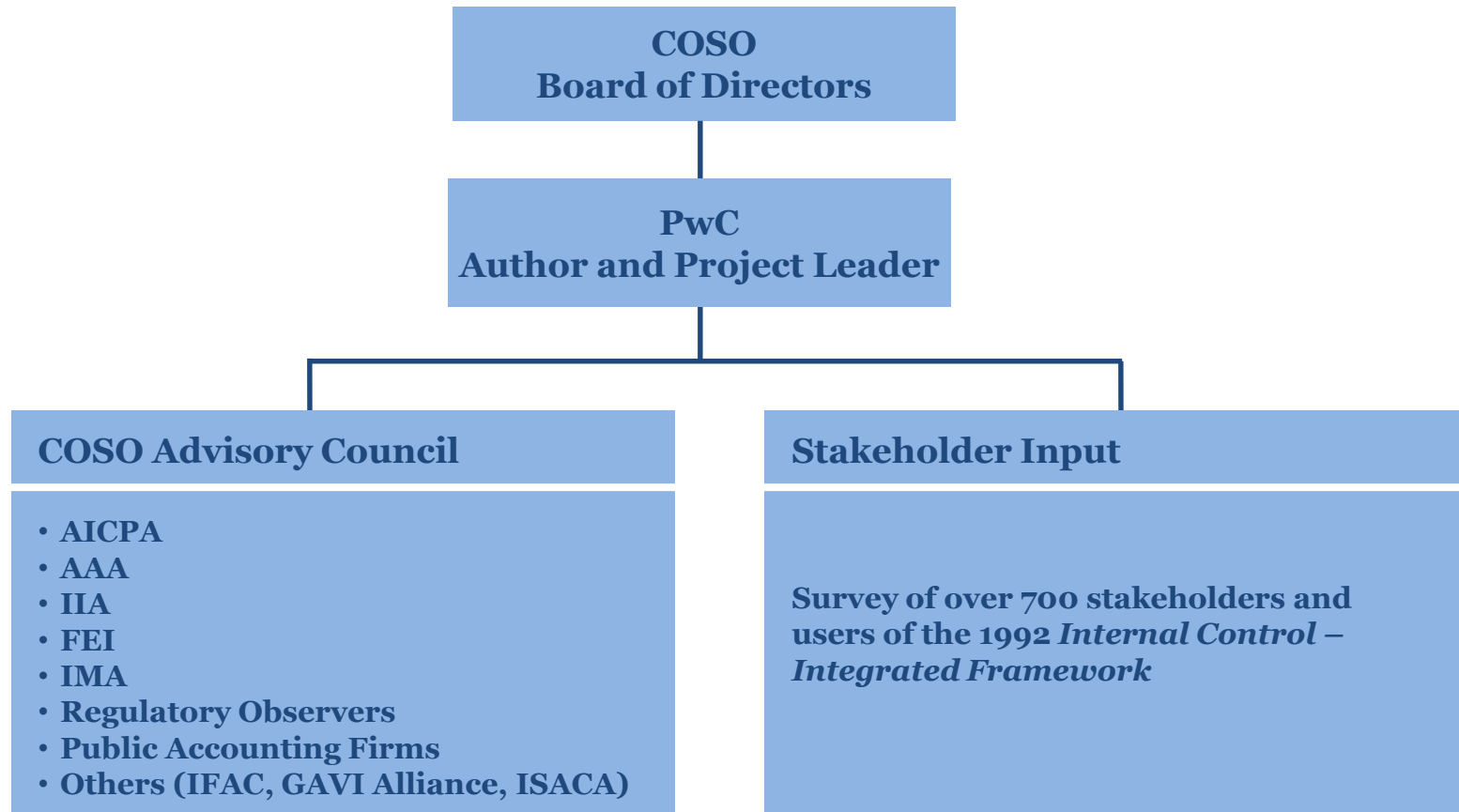
- First published in 1992
- Gained wide acceptance following financial control failures of early 2000's
- Most widely used framework in the US
- Also widely used around the world



Original COSO Cube

Update on Revisions to the COSO Framework for Internal Controls

Project Participants



Update on Revisions to the COSO Framework for Internal Controls

Summary of Updates

What's changed...

The experienced reader will find much familiar in the updated *Framework*, which builds on what has proven effective in the original version.

What is not changing...

1. Definition of internal control
2. Five components of internal control
3. The fundamental criteria used to assess effectiveness of systems of internal control
4. Use of judgment in evaluating the effectiveness of systems of internal control



What is changing...

1. Codification of principles with universal application for use in developing and evaluating the effectiveness of systems of internal control
2. Expanded financial reporting objective to address internal and external, financial and non-financial reporting objectives
3. Increased focus on operations, compliance and non-financial reporting objectives based on user input

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Summary of Updates

A changing business environment... Drives updates to the Framework...

Expectations for governance oversight

Globalization of markets and operations

Changes in business models

Demands and complexity of rules, regulations and standards

Expectations for competencies and accountabilities

Use and reliance on evolving technology

Expectations for preventing and detecting fraud



Updated COSO Cube

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Summary of Updates

Codification of 17 principles embedded in the original Framework

Control Environment

1. Demonstrates commitment to integrity and ethical values
2. Exercises oversight responsibility
3. Establishes structure, authority and responsibility
4. Demonstrates commitment to competence
5. Enforces accountability

Risk Assessment

6. Specifies relevant objectives
7. Identifies and analyzes risk
8. Assesses fraud risk
9. Identifies and analyzes significant change

Control Activities

10. Selects and develops control activities
11. Selects and develops general controls over technology
12. Deploys through policies and procedures

Information & Communication

13. Uses relevant information
14. Communicates internally
15. Communicates externally

Monitoring Activities

16. Conducts ongoing and/or separate evaluations
17. Evaluates and communicates deficiencies

FEI's Working Group on COSO: Comment Letter

- **April 2, 2012: Comment letter submitted to COSO**
 - *RE: COSO Exposure Draft, "Internal Control-Integrated Framework" (Dec. 2011 ED)*
 - *Submitted to David Landsittel, Chairman of COSO*
 - *Signed by Ray Purcell, Chairman of FEI's Working Group on COSO*

FEI's Working Group on COSO: Comment Letter

- **Support for Update of 1992 Framework; Principles-Based Approach**
 - *FEI's WGC strongly supports the continued use of the five (5) core components of internal control*
 - *FEI's WGC believes the 17 principles in ED as underlying of five (5) core components are reasonable and helpful in discussing and applying framework*

FEI's Working Group on COSO: Comment Letter

- **Improvements Can Be Made to the ED, to Reduce Risk of Unintended Consequences**
 - *FEI's WGC supports the objective of project:*
 - *"This project is not intended to change how internal control is defined, assessed, or managed, but rather provide more comprehensive and relevant conceptual guidance and practical examples."*
(excerpt from COSO's Nov. 18, 2010 press release)
- *FEI's WGC has concern that the ED as currently written, including the role of the 81 'attributes' supporting the 17 'principles' may encourage a 'checklist' approach, and may pose significant risk of unintended consequences*

FEI's Working Group on COSO: Comment Letter

- **Concerns**

- *FEI's WGC remain concerned that insufficient time was provided in the comment period*
- *To address this concern, FEI's WGC recommends that COSO re-release a revised ED (revised to address public comments on the initial ED), concurrent with the release for public comment of any additional volumes currently contemplated and under development by COSO to accompany the core framework ED, such as Evaluation Tools and Approaches and Examples on Internal Control over External Financial Reporting.*
- *FEI's WGC recommends:*
 - *Conduct certain due process procedures to enhance public visibility of, and input on, the ED's*

FEI's Working Group on COSO: Comment Letter

- *FEI's WGC recommends to make certain improvements to the framework ED and other upcoming volumes that are integrally related to the ED, to reduce the risk of unintended consequences.*
 - *Carefully describe the nature of these other documents*
 - *Segregate guidance (the 'framework', or de facto 'standards') from ancillary material such as illustrations, detailed 'thought leadership' expanding on the guidance, and tools*
 - *Clarify, in particular, that attributes are not equivalent to principles and that they may be viewed as good practices rather than as standards or even best practices*
 - *Clarify that the evaluation of the system of internal control over financial reporting continues to carry forward the approach in the 1992 framework emphasizing the five components of internal control taken as a whole*
- *FEI's WGC recommends clarify the board's oversight role vs. management*

FEI's Working Group on COSO: Comment Letter

- **Due Process is Key**

- *FEI's WGC recommends:*

- *Address transition issues (directly or indirectly, if to be acted on by regulators)*

What's Next

- **April 30, 2012: COSO Press Release**
 - *“COSO Expects to Issue the Updated Internal Control-Integrated Framework and Related Supporting Documents During the First Quarter of 2013”*
 - *“We are pleased to receive comment letters from so many organizations and professionals,” said David Landsittel, Chairman of COSO. “We recognize there is a diversity of input and we need to fully consider these observations and suggestions before issuing the updated Framework.”*

What's Next

- **April 30, 2012: COSO Press Release**

- *In addition to updating the Framework, COSO and PwC are developing*
 - *a related compendium of approaches and examples that illustrate how the principles set forth in the updated Framework can be applied in designing, implementing and maintaining internal control over external financial reporting*
 - *related evaluation tools to use in assessing effectiveness of internal control. COSO expects to release final copies of all three documents 2 of 2 during the first quarter of 2013, and during the interim months, public comments will continue to be solicited.*

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