

## Heads Up

### In This Issue:

- COSO Framework
- Internal Control Over External Financial Reporting
- Submitting Comments

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## COSO Releases Exposure Draft of Updated Integrated Framework on Internal Control

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On December 19, 2011, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) released an [exposure draft](#) (ED) of its updated *Internal Control — Integrated Framework* (the “framework”) for public comment. COSO anticipates finalizing and publishing the revised framework in late 2012.

The framework was initially published in 1992 and has since become one of the most widely accepted internal control frameworks in the world. COSO's primary objective in updating and enhancing the framework was to ensure that it continues to be relevant to stakeholders in light of the significant changes to business and operating environments over the past 20 years.<sup>1</sup>

COSO has retained aspects of the original framework. For example, the definition of internal control, the three categories of objectives (effectiveness and efficiency of operations, reliability of reporting, and compliance with applicable laws and regulations), and the five components of internal control (control environment, risk assessment, control activities, information and communication, and monitoring activities) have remained unchanged.

In addition to the framework, the ED contains an executive summary geared toward boards of directors, senior executives, and regulators.

### COSO Framework

As described in the ED's executive summary, one of the most significant enhancements to the original framework is the codification of its internal control concepts into 17 principles and 81 supporting attributes. These principles and attributes are similar to and build upon those published in COSO's 2006 guidance *Internal Control Over Financial Reporting — Guidance for Smaller Public Companies*.

In addition, COSO broadened the original framework's financial reporting objectives to include those related to both financial and nonfinancial reporting and internal and external reporting. The revised framework also focuses more closely on fraud and includes considerations related to the potential for fraud as a principle of internal control. Also, COSO refreshed certain concepts and made enhancements in response to significant changes in the business environment, such as globalization, increased regulatory oversight, and increased reliance on technology.

<sup>1</sup> COSO engaged PricewaterhouseCoopers LLP (PwC), which participated in developing the original framework, to lead the update project. In addition, COSO assembled an Advisory Council with industry practitioners and representatives from academia, government agencies, and nonprofit organizations to advise it throughout the ED's development. Representatives from various regulatory agencies, including the FDIC, GAO, IFAC, PCAOB, and SEC, have also participated as observers at Advisory Council meetings. Moreover, COSO sought and received input from over 750 survey respondents on the scope of the project and the extent of the revisions.

All financial statement stakeholders, including audit committees, company management, and investor groups, are encouraged to study the ED and submit comments to COSO by March 31, 2012.

The 17 principles in the revised framework represent the fundamental concepts associated with each of the five components of internal control. All of the principles apply to each of the three categories of objectives (operations, reporting, and compliance) and to the individual objectives within each category. Each principle is supported by attributes that represent characteristics associated with that principle. The principles and attributes are intended to be used by management as criteria to assess whether internal control is effective. Appendix B of the ED describes additional enhancements to the framework.

## Internal Control Over External Financial Reporting

COSO does not expect the revised framework to change current internal control attestation processes because the applicable principles and attributes were encompassed in the original framework. COSO also plans to release a supplemental publication, *Guidance on Internal Control Over External Financial Reporting* (ICEFR), for a 60-day comment period in early spring or summer of 2012. The supplemental publication would provide guidance on applying the revised framework to ICEFR and would link the principles and related attributes in the revised framework to relevant approaches to and examples of external financial reporting objectives. COSO's *Guidance on Internal Control Over Financial Reporting — Guidance for Smaller Public Companies*, originally issued in 2006, will be superseded by the supplemental guidance on ICEFR. COSO plans to release both the final revised framework and the new supplemental guidance on ICEFR at the same time in late 2012.

**Editor's Note:** COSO has not announced plans to revise its *Enterprise Risk Management — Integrated Framework*, issued in 2004, or its *Guidance on Monitoring Internal Control Systems*, issued in 2009.

## Submitting Comments

All financial statement stakeholders, including audit committees, company management, and investor groups, are encouraged to study the ED and submit comments to COSO by March 31, 2012. Interested parties can provide feedback on [the ED](#) by answering a [set of questions](#) or by [uploading their comments](#) as an attachment.

Consideration of the following questions and others may help readers evaluate the ED and develop feedback:

- Will the updated framework help strengthen an entity's systems of internal control?
- Is the updated framework internally consistent and logical?
- Is the updated framework written in a manner that is understandable and easy to use?
- Are the 17 principles in the updated framework a complete set of principles?
- Is the framework overly prescriptive in suggesting that all 17 principles should be present and functioning?
- Can an entity conclude that it has effective internal control if one or more of the 17 principles are not present and functioning?
- Does the updated framework appropriately expand the reporting objective category (i.e., internal and external reporting, financial and nonfinancial reporting)?
- Does the updated framework appropriately balance the reporting, operations, and compliance-related approaches and examples?
- Does the updated framework appropriately take into account the implications of the expanded role of technology in organizations?
- Does the updated framework appropriately emphasize risks and controls related to fraud?
- Does the updated framework provide sufficient guidance on determining whether a deficiency exists and, if so, on assessing the severity of deficiencies?

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