PCAOB
Public Company Accounting Oversight Board

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December 15, 2006

The Honorable Christopher Cox
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chairman Cox:

I am pleased to transmit summaries of the Public Company Accounting Oversight Board's most recent performance reviews, conducted by the Board's Office of Internal Oversight and Performance Assurance (IOPA). The Board formed IOPA to provide assurance to the Board, the Securities and Exchange Commission, and other interested parties that the PCAOB is achieving the objectives of Title I of the Sarbanes-Oxley Act in an effective manner. IOPA conducts its reviews in conformance with Government Auditing Standards issued by the Comptroller General of the United States.

The reviews discuss three aspects of the Board's information technology activities: investment review; document management; and enterprise architecture. In each case, IOPA's recommendations are based, in part, on industry and government best practices.

As part of the PCAOB's strategic planning process, the Board plans to ensure that future information technology investments are aligned with its strategic goals and objectives, and provide secure, reliable and cost-effective support for our operations. A recently-established information technology advisory group, whose members include the PCAOB's senior leadership, will assist the Board in this endeavor by recommending governance policies, processes, and strategies that are consistent with best practice for information technology and appropriately scaled to the PCAOB's business needs.

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The Board intends to publish the attached summaries of IOPA's reviews on the PCAOB's Web site on or about December 19, 2006. Please contact me or the Director of IOPA, Peter Schleck (202-207-9115), if you have any questions about the reviews.

Sincerely,

Mark Olson

Mark W. Olson
Chairman

Enclosures

cc: The Honorable Paul S. Atkins
The Honorable Roel C. Campos
The Honorable Annette L. Nazareth
The Honorable Kathleen L. Casey

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PERFORMANCE REVIEW

THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD'S INVESTMENT REVIEW COMMITTEE (IOPA-2006-004)

INTERNAL OVERSIGHT AND PERFORMANCE ASSURANCE
December 12, 2006

Objective

Consistent with its 2006 review plan, Internal Oversight and Performance Assurance (IOPA) conducted a risk assessment of the Public Company Accounting Oversight Board's (PCAOB, or the Board) information technology (IT) activities. IOPA presented the results of the risk assessment to the Board in June 2006, and proposed at that time to conduct follow-on reviews of the PCAOB's investment review committee (IRC), enterprise architecture project, and document management. The Board approved this proposal and IOPA subsequently met with the Chief Administrative Officer (CAO) and Chief Information Officer (CIO) to discuss the approach and methodology for conducting the reviews.

This report discusses the IRC.[1/] The review objective was to determine whether the IRC's composition and procedures were consistent with best practices for IT investments.

Background

Since its inception, the PCAOB has invested about one of every four dollars expended in information technology. By the end of 2006, the total IT investment will approximate $93 million. About one-third of this investment has been for contractors hired to assist in the development of the PCAOB's web-based registration, billing, and

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[1/] This is a public summary of the report. The full report, prepared in accordance with Government Auditing Standards, has been issued to the Board. The full report includes a detailed discussion of the review objective, scope, and methodology.

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other systems. Twenty-five percent is attributed to staff salaries for the Office of Information Technology (OIT), which included 74 regular employees and 6.5 additional full-time equivalent contractor staff, as of August 2006. An additional 25 percent has provided for security, servers, and related software. Finally, 16 percent of the investment provided for the hardware, software, telecommunications, and network capabilities to support a PCAOB staff that has grown from just a few employees in 2003 to 448 in late 2006.

In November 2004, IOPA issued a report on *Internal Control Review of the Public Company Accounting Oversight Board's Information Technology and Security Function* (IOPA-2004-002). In that report, we made a number of recommendations regarding the further development of IT governance models and processes to help ensure appropriate control over the Board's technology investment. Relative to those recommendations, IT has adopted various governance models, documented additional procedures, and was continuing to work on an enterprise-wide architecture and performance metrics.

The IRC was formed in late 2004 as an internal control to ensure the strategic alignment of information technology projects. As described in the PCAOB's draft 2006 information technology business plan, the Chief Administrative Officer created the IRC to "… review all proposed project activity to ensure organizational alignment with the board's mandate, budget and resources. The IRC is a strategic internal control from both a financial and operational management perspective." The business plan further notes that the IRC, which meets as required to review proposed information technology activity, is made up of three standing members: the CAO, the Chief Financial Officer (CFO), and the CIO.

The IRC is also described in a draft Office of Information Technology policy dated December 8, 2004. The draft policy outlined a process by which proposed technology projects would be subjected to committee review at various development checkpoints. Each project was to be "properly reviewed" to ensure alignment with strategic business objectives from inception; cost/ benefit prior to development; and, successful requirement implementation prior to deployment. The IRC's decision options outlined in the draft policy included approving, ending, or deferring projects and requesting additional information.

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Best Practices for IT Investments

Frameworks developed by the IT Governance Institute (Institute)[2/] and by the U.S. Government Accountability Office (GAO)[3/] stress the importance of ensuring that IT projects are tightly aligned with the organization's business needs. The Institute's framework specifically notes that alignment of IT with overall strategic objectives requires full and active involvement from many levels and activities within an enterprise. Proactive involvement by the organization's Chief Executive Officer (CEO) and board is considered essential for ensuring the establishment of an IT strategy that is aligned with business requirements and that IT delivers value consistent with the organization's strategic objectives.

Investment committees are an accepted best practice for helping the CEO and board achieve and maintain IT and business strategy alignment. GAO considers the establishment of an IT investment committee[4/] a fundamental building block in its IT investment maturity model. The GAO model stresses the importance of a documented investment process, and contemplates that the investment committee will have oversight responsibility for ensuring that the process is followed. GAO indicates that the investment committee should be composed of senior executives from IT, financial management, and business units. Depending on an organization's size, more than one IT committee may be appropriate, but any "subordinate" committees should have the same broad representation.

Likewise, the Institute's framework contemplates one or more committees to help govern IT, including an IT investment committee. In this framework, the investment committee considers and approves IT projects, and is responsible for ensuring that a robust business case is made and that alignment issues are fully addressed. To successfully optimize business alignment, according to this framework, the committee should be properly representative of all major operating and support departments. The framework also acknowledges that delegation of responsibilities to lower-level

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[2/] The IT Governance Institute is a non-profit research organization supporting the global business community. Its framework for IT investment is discussed in: *Optimizing Value Creation from IT Investments*, 2005; see also, *IT Alignment: Who is in Charge?*, 2005.

[3/] *Information Technology Investment Management: A Framework for Assessing and Improving Process Maturity*, GAO-04-394G, March 2004.

[4/] GAO uses the term "investment board." The term "committee" is used in this report to avoid confusion with references to the PCAOB board.

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personnel will weaken the committee's effectiveness. Nevertheless, the Institute's materials stress that investment approval committees with representation from both business and IT helps to ensure that decisions are made with neutral bias and with proper transparency. Furthermore, the Institute contends, IT is not an end in itself but supports and enables the business. As such, IT strategy setting and implementation should include business leadership.

Both of the frameworks cited specifically note that there is no single approach to IT investment management and alignment that meets the needs of all organizations.

Such factors as the entity's nature and size, its dependence on IT, and its leadership and culture influence decisions regarding how best to manage IT. At the PCAOB, the CEO and Board are ultimately responsible for IT, and therefore choose the tools and structures for investment management they deem most appropriate.

Results of Review

The members of the IRC deserve credit for establishing a control mechanism that adds discipline to IT investment decision-making. However, the IRC is not fully consistent with best industry or government practices because it does not include business unit[5/] representation and its processes are not well documented. In this regard, PCAOB division staff and some Board members we interviewed told us they did not have a clear understanding of IRC objectives, decision-making criteria and rationale, or operations. Division directors and staff, in particular, expressed frustration at what they perceived as the IRC's lack of transparency.

The CAO expressed some concern that widening the IRC's membership to include business units could delay the investment review process, particularly if division directors failed to regularly participate or delegated some of their responsibilities to others. The CAO also indicated that policy-level discussions that bear on the IT investment decision process have been delayed by transitions in Board leadership. Now that a new chairman has been appointed, the CAO intends to facilitate such discussions.

In our judgment, an IRC process that includes wider participation by business units and better documentation offers potential benefits to PCAOB operations and also

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[5/] In this report, "business units" refers to the offices and divisions of the PCAOB. For example, the Office of Chief Auditor would be considered a business unit.

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helps to demonstrate the Board's commitment to transparent stewardship of funds provided by registrants and issuers. Strategic involvement by the Chairman (and Chief Executive Officer) and Board members is critically important to ensure that the IRC has the right composition and processes in place to help the PCAOB maximize the effectiveness of its substantial investment in information technology. The full report included recommendations consistent with our observations.

In a consolidated written response addressing all three of IOPA's IT-related reports, the then-CAO and the CIO outlined a series of proposed steps which, if implemented, would be generally consistent with the intent of our recommendations.