August 11, 2006

Rule-Comments@sec.gov
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Mr. Chairman and Honorable Commissioners:

Thank you for the opportunity to respond to your ***Concept Release Concerning Management's reports on Internal Control over Financial Reporting***. Your introduction summary to the Release indicates that any future guidance is to be influenced by the nature and extent of public interest and the needs and concerns of public companies.

Your list of topics for discussion may assume a mature subject that now only needs refinement through your guidance; and the presentation of the matters in each topic seems based on a conclusion that the first reaction (Sarbanes-Oxley) now needs to be "reined in" to relieve the burden on registrants. Keep an option open that neither assumption is true.

The current problem of executive compensation, including backdating of stock option pricing reveals a problem. The problem was not discovered because of changes made in 2002 which required more vigilant audits, better internal controls, CEO and CFO certification, increased independence of audit committees including financial experts. Unfortunately, uncontrolled executive compensation is only one of many examples, but the most influential because it is in this morning's headlines. Daily business news suggests that the problem is visibly not yet solved, not even identified. Most importantly, the internal control emphasis did not work. Now, it appears we are all just waiting for the next failure of a recently repaired system.

Good things have been done, but some of what has been done is only "feel good" activity that does not help. Many have contributed with great sincerity, but we are not at a point yet to relax. We should be concerned with suggestions that we can now be comfortable.

An opportunity!

In that regard, your announcement on August 9, 2006, of an additional extension of time for smaller public companies and foreign private issuers to comply with Section 404 may tip a preference for "needs and concerns" of public companies compared to the "public interest." But, it does offer an opportunity. By the earliest time public information and reports about internal controls will be available for these exempt entities, constituting 44% of U. S. public companies, nearly six years will have passed since Sarbanes-Oxley became law. You and we will have a gigantic database of public companies that complied with 404 and a control group of those who did not. Who won? That information, together with the pre Sarbanes Oxley years of experience should offer significant hindsight review of the effect SEC oversight and direction has had on quality of controls since the Great Depression. The Government Accountability Office should be engaged now to begin the study.

There are some simple truths.

First, there are no engineered systems of internal controls; we should not pretend there are. Some companies have some good control techniques, now better documented because of Sarbanes-Oxley. But, they are not engineered, tested, dynamic systems. We should not have suggested regulation is based on something that is not there.

Second, complex systems and situations require good controls to work properly and safely. That need is not muted because they are owned by smaller companies with less capital, and fewer managers with broader spans of control. There is a cost to being a public company and control should appropriately part of it.

Third, some entities should not have access to public markets to raise capital. Such access is a sensitive privilege that should be reserved for very responsible organizations. CPA's, lawyers, investment bankers, directors and regulators that enable remote, public ownership of company securities, accept great responsibility when they promote public positioning and the liquidity and wealth provided by those markets.

Fourth, some among us are greedy and pathological, and all make mistakes. That has always been true and will not change. Some business schools teach greed and pathology. We can't reverse human nature and advanced education with two day seminars on ethics.

Fifth, the big 4 accounting firms are not properly capitalized and organized to provide comfort intended by their certifications of management certifications, even if they are "registered" by the PCAOB. They now audit public companies that account for 98% of public company revenues. The PCAOB should probably spend 98% of its time on them. Everything we have seen says they need to be better controlled. They have been unable to do it themselves. Their partners, most of whom are wonderful people, are not exempt from greedy and pathological behavior. And, they make mistakes, like we all do.

Sixth, we are not losing our edge because more IPO's are moving to non U.S. jurisdictions. The offshore movement may be a warning, but probably not that our standards are too high. If global markets and exchanges are inevitable, let's hand off a good model, not spread a disease.

Answers are clear.

We must think about controls differently. A culture exists that promotes finding and fixing, rather than anticipating and preventing. Many would disagree with that assessment, but consider the backdated stock options issue. Why did no one responsible for controls at the many companies where the problem occurred ever raise the question, anticipate that it would happen, and install a simple fix so that it could not happen? Accountants and auditors who know the accounting rules have been looking at these transactions for years. Some of the perpetrators of these schemes were accountants and former auditors, now CFO's. Where were they when Sarbanes Oxley provisions were applied? More importantly, what else has been missed?

Internal Controls—The public has a right to expect tested development of controls. Regulator requirements for reviews, that imply something exists when it does not, do not substitute for the real thing. Further "guidance" of what you want on this approach succeeds only in narrowing what little protection the public has. If companies had invested all the money spent on external audits since 1933 on understanding and developing controls, external audits would be easier to do and more reliable. Perhaps they would not be necessary. We might, then, have had universities offering courses on controls, rather than forensic classes on how to search for and document fraud. We would all be better served. Airplanes get grounded; cars get recalled; the "big dig" is closed. Securities of public companies with weak controls should be suspended from trading. Reports on internal controls, if we have reports, should be about the future. The report language "…as of…" a date three or four months ago means little when annual reports are mailed to the public. When I get on a jet passenger plane, I assume the thing worked for the flight that just ended. I want to know that someone has checked out controls for the flight I am going to make. The FAA requires it. Financial controls of a company are no different. Are the controls ready for the foreseeable?

Human nature—Control for the weaknesses of human nature. It can keep good, creative people out of jail, without Presidential pardon. Management override of controls should be made impossible. Don't spend another nickel trying to change in a couple of years what world religions have been unable to fix for millenniums. Much of the current management response is no more than PR. Defendants find religion as a trial tactic. One major transgressor required that 250,000 employees go through ethics training because some top executives and board members predictably couldn't behave: the "Dilbert" approach. What did stockholders gain from that?

Non-accelerated filers—The dividing line is whether the company is public or not. Controls should be a serious consideration whenever a company goes public. We are not simplifying a problem or solving it by creating a multi-layered system and standards for similar facts. There is inconsistency in suggesting that smaller companies can take longer to give information to investors and that their complex systems can be approached less formally. Why?

Responsibility to the Public---Few security holders have access to anything other than what is filed with the Securities and Exchange Commission. They and the market have every right to believe that information has been carefully accumulated and reported, using a control system that has been properly designed to anticipate the foreseeable. It is what public companies are supposed to do, regardless of company size. The public is tired of suggestions (or "guidance") that some shield or safe harbor ought to be in place for those receiving fees and salaries for being part of and close to the deal. Retirees with poorly funded defined benefit plans would like a safe harbor too, but the PBGC is shaky, mostly the result of reporting and control problems by plan sponsors. Directors should be paid regardless of company earnings. Whether paid or not, they should be exposed to all the consequences of bad oversight.

Registered Public Accounting Firms--- Set some standards for adequate capitalization relative to the aggregate work undertaken and firm history of performance and responsibility. When the accounting firms were relieved of "joint and several" liability in favor of proportionate liability, and permitted to organize as limited liability structures, common sense should have suggested requiring an adequate level of capitalization and clear disclosure of financial strength, not to make them juicy targets but to indicate the level of commitment by their owners. Accounting firms' intangible assets, people and client relationships, are far too fluid for investor and public company comfort without adequate capital commitment. A proper level of at risk capital for each owner will help assure a proper level of professional effort, including the effort needed for a proper evaluation of internal controls. For the public interest, internal control reporting by the firms should be a great responsibility, not just a revenue opportunity. Make them report their financial condition and insurance coverage to the Securities and Exchange Commission.

Thank you for your continuing search for the better protection for investors.

Sincerely,

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