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April 1, 2005

**VIA E-MAIL**

Mr. Jonathan G. Katz  
Secretary  
Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

Re: Feedback on Section 404 (File No. 4-497)

Dear Mr. Katz:

Forest City Enterprises, Inc. (FCE or Company) welcomes this opportunity to respond to the request for feedback from the Securities and Exchange Commission (SEC or Commission) on the implementation of Section 404 of the Sarbanes-Oxley Act of 2002 (the Act). FCE is a publicly traded (NYSE: FCEA and FCEB) corporation engaged in the ownership, development, management and acquisition of commercial and residential real estate throughout the United States.

FCE commends the Commission for actively pursuing feedback and recommendations to improve and streamline the requirements of Section 404 of the Act (Section 404). Our experience with Section 404 has had some positive results including improved documentation of our business processes, identifying areas for process improvement, reinforcing the importance of an effective control environment and creating an entity wide awareness of the importance of each employee's day-to-day tasks and procedures to the Company as a whole.

Although we had some positive experiences with Section 404, these were offset by the enormous costs, both external and internal, and the huge burden put on our employees' current workload. We feel we have always had a high degree of integrity over our financial reporting process. As such, we do not feel the benefits derived from becoming Section 404 compliant exceeded the enormous costs incurred to comply. We have summarized our concerns under the current guidance below and believe that if the concerns are alleviated, that significant cost savings can be achieved without compromising the intent of the Act.

## **SUMMARY OF CONCERNS AROUND SECTION 404 COMPLIANCE**

1. To reduce the external and internal costs of control testing, FCE requests the Commission to consider providing guidance around the scope of testing and/or the testing approach for both management and its auditors to reduce the overall costs of compliance. The following examples are provided for the Commission's consideration:

### **Scope Considerations:**

- a. Two of the five IT general computer control domains (back-up and recovery and data center operations) have risks that primarily relate to disaster recovery. The Commission should consider eliminating these domains for testing as disaster recovery has been deemed out of scope for Section 404 compliance.
- b. Further guidance for management and its auditors is needed for the evaluation of the controls around end user applications (spreadsheets) and segregation of duties.
- c. Consistency across the audit firms is needed for controls around baselining of system reports and calculations. The baselining process is more of a substantive test rather than a test of controls. Some firms require that management perform these substantive tests while other firms do not appear to consider them to be in-scope for compliance testing.

### **Testing Approach Considerations:**

- d. To reduce the burden on our employees and excessive costs associated with redundant testing of controls, FCE suggests that the Commission consider allowing the combination of management and its auditor's testing to fulfill the testing scope for a control where the auditor plans to rely upon management's work. FCE's experience for compliance testing has been where management tests the full sample (e.g. 60 transactions) of a control and the auditor tests at least an additional 15 transactions to satisfy the principle evidence provision. The costs associated with testing the additional 15 transactions in management's testing could be eliminated without impairing management's ability to assess the effectiveness of the control or comprise the auditor's requirements to satisfy the principle evidence provision.
- e. The standard of documentation required to prove a control was performed, especially a management review control, is very burdensome. Auditing standards consider inquiry, observation, inspection of documentation and re-performance as appropriate tests of controls. The Commission should consider providing substance over form guidance, such as whether a signature along with inquiry procedures could be used to support that a review by management was performed, to reduce the overall costs of compliance. Retaining volumes of documents with review tickmarks and explanations of exactly what was performed to allow an independent auditor to re-perform the control is time consuming and not cost effective.

2. The evaluation of control effectiveness is very stringent. Currently, one or two exceptions out of sixty requires management and its auditor to conclude a control is ineffective, yet these results indicate the control operates effectively over 90% of the time. We would like the Commission to consider lowering the tolerance level of exceptions when evaluating whether a control is effective.
3. The framework for evaluating deficiencies at the process/transaction level does not allow a company to take credit for other pervasive detect controls that are not considered key and tested (i.e., senior management analytical reviews, budget to actual reviews, etc.) prior to the deficiency rising to the level of significant deficiency. Consideration should be given to modifying the framework to allow for pervasive qualitative factors to be considered by a prudent official prior to the exception already reaching the level of significant deficiency.

FCE thanks the Commission for this opportunity to comment on the implementation of Section 404 of the Sarbanes-Oxley Act and offer some suggestions for consideration that we feel will reduce confusion, streamline the process, improve standardization of compliance measures and reduce both internal and external costs of compliance. We believe these benefits can be derived without compromising the underlying theme of strengthening internal controls over financial reporting. Please contact Chuck Obert, Vice-President of External Reporting and Project Manager of Section 404 compliance at (216) 416-3318 or myself at (216) 416-3201 if you would like to discuss our comments.

Respectfully submitted,

Thomas G. Smith  
Executive Vice President, Chief Financial Officer and Secretary