IssuesCentral

April 8, 2005

File No. 265-23

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

Subject: Comments for the SEC Advisory Committee on Smaller Public Companies

Dear Mr. Katz:

We appreciate the opportunity to submit our comments to the Advisory Committee on Smaller Public Companies prior to the first meeting on April 12, 2005.

Our organization, Issues Central, Inc., was created with the mission to provide leading products and techniques to facilitate effective and efficient financial compliance (in accordance with legislation such as the Sarbanes-Oxley Act of 2002) for mid to emerging public companies. Our comments in this letter are based on practical industry experience with firms listed on all major exchanges in North America.

In keeping with the Committee's mandate we are focusing our comments on the Committee Charter of March 3, 2005 - Objectives and Scope of Activities outlined in Section B, Points 1 through 3.

First Principles – Setting the Context:

Principle 1 - Investor trust is priceless

Principle 2 - American financial markets are responsible for safeguarding the largest percentage of the world's investments

Principle 3 – Well-managed small companies of today working within a fair and balanced legislation environment have an opportunity to become the dominant enterprises of tomorrow, therefore

Principle 4 – Investors and small companies will both be well served if clear and pragmatic set of checks and balances are implemented with respect to internal controls and certifications.

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Immediate Actions – For Your Consideration:

Action 1 – A careful assessment of whether there should be different treatment, or standards, for the validation of effective internal controls and reporting for a "smaller" company as opposed to a "larger" company with more resources. A review of key attributes and organizational characteristics of smaller firms, and their implications for internal control and reporting processes would be helpful. Some general observations we would submit to the committee with respect to smaller firms are as follows:

- *Tone At The Top*- Smaller companies tend to be more entrepreneurial and driven by a "take the hill" attitude. Society cannot afford to choke off this energy, drive and nimble approach to growth. At the same time, the emphasis is not on controls. Executives at smaller organizations need to believe that they can build effective and cost efficient control in-line with their processes. This is going to take significant effort.
- *Segregation of Duties* – Smaller companies do not have the level of administrative staffing found in larger organizations. Job descriptions often require that an employee where "multiple hats". Segregation of duty concerns are inevitable. Some of these concerns can be dealt with through more thoughtful process design – but not in all cases. In many cases, there are just too few people to go around for perfect controls. Perfect controls may put a company out of business.
- *Information Technology Controls* – Systems are often more informal in a smaller organizations. They are more likely to be a combination of spreadsheets and an accounting system that allows tremendous control over data before and after posting.
- *Level of Staff Expertise and Training* – Generally smaller organizations do not have the "bench strength" with regards to effective and efficient control processes. The internal audit function is not staffed in many smaller companies. In addition, the human resources function may not exist as a separate department, but is often incorporated into the activities of operations management. Training programs and ongoing skills investment in people are minimal in many cases. The net effect of these characteristics is that there will be more opportunity for control issues at the entity-level.
- *Management's Understanding of Day-to-Day Operations* – Management teams at smaller companies are more in touch with operations and the reality of the business' activities. This should provide a significant advantage with respect to many aspects of internal control when compared with the multi-level insularity of many management teams at larger organizations from their operations.

Action 2 – If there is to be a more modest implementation and validation of internal controls for smaller companies then what is to be the definition of "smaller"? As of today, a market capitalization of $75M or less has been the measure for a longer implementation timeframe with respect to components (i.e. – Section 404) of the

Sarbanes-Oxley Act of 2002. Does capitalization as the primary criteria for "small" make sense? There will be no perfect measure, but some issues for discussion might include:

- *Annual revenue* – While this is typically used as a gauge of business size, there are many early-stage organizations (R&D, life sciences, natural resource, etc) that have significant market capitalization with little or no revenue. To what extent should revenue be considered as an indicator of the ability to implement stringent internal controls and validation processes?
- *Number of employees* – A common complaint of smaller organizations is that they do not have the staff to support "big company" control and compliance processes. Is there a way to effectively link staffing levels as a gauge of ability to undertake more robust control and reporting requirements?
- *Number of Shareholders* – A central principle is to protect investor confidence. Perhaps if an organization has a very limited number of shareholders then the issue of extensive internal controls validation is less relevant as the shareholders are often quite close to the daily activities of the business.
- *Other Considerations* – Length of time on public markets might be considered to provide new market players with a transition time to implement fully featured internal controls and reporting regimens.

The Committee has an ambitious and important mandate in the coming months. On behalf of mid size to emerging/smaller companies we would like to provide the committee with the following recommendations for all parties to consider:

Recommendations – For Smaller Companies

Recommendation 1 – Do not procrastinate and do not anticipate that there will be more relaxed standards for your organization. Start now. Leaving compliance work such as the implementation of your initial Section 404 work too late will cause you to use become overly dependent on outside resources. This will undermine quality and longer-term ownership over effective internal controls, and drive up the cost of compliance.

Recommendation 2 – Develop an internal controls/404 "playbook" by planning and scoping your project completely and thoroughly before getting into the details and undertaking testing. The old adage of "Measure twice, Cut once" applies and will help you create a strong foundation for subsequent years.

Recommendation 3 - Do not become dependent on outsiders during the implementation of your initial controls work. Involvement of your staff is critical. As a management team you are the overall process owners. By building effective internal controls "in-line" with your processes you will build a more prosperous enterprise for shareholders, customers and employees. You also will over time drive the cost of compliance down and the benefits up.

Recommendation 4 – Build into your company's culture the attitude that sensible controls are good business and reduce unnecessary risk. You should consider the COSO ERM framework as a way to promote good controls and good business.

Recommendations – For Legislators/Standards Committees

Recommendation 1 – Develop a clearer set of guidelines for the audit profession with respect to interaction with clients and their reliance on client control documentation. Further, clarify the ability of the auditor to provide advice around controls to the client as this will help smaller companies achieve compliance in a more cost effective manner. As of today, both auditors and clients are erring on the side of extreme conservatism and thus driving up the cost and increasing fear and frustration.

Recommendation 2 – Provide guidance to auditors on the ability to use a higher percentage of detective controls versus preventative controls. This will help to address the smaller organization's more limited staffing structure.

Recommendation 3 – Provide more specific guidance to smaller firms with respect to entity-level controls. For example, the use of management meetings and documented minutes to cover areas such as the control environment; human resource policies and procedures; information and communication; and monitoring. This is in contrast to larger organizations that have more structured policy manuals; internal "intranets", etc to formalize the same entity-level controls.

We wish the committee a productive meeting and look forward to discussions that will forward the interests of both investors and smaller organizations.

Please contact me directly at 800.410.6681 ext 114 if you require additional input on the items above.

Sincerely,

Catherine Connally, CIA
President
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