INSTITUTE OF MANAGEMENT ACCOUNTANTS

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April 3, 2006

Nancy M. Morris
Federal Advisory Committee Management Officer
Securities and Exchange Commission
100F Street NE
Washington, DC 20549-1090

RE: FILE NO. 265-23 Exposure Draft of Final Report of the Advisory Committee on Smaller Public Companies

The Institute of Management Accountants (IMA®) is the world's leading nonprofit association representing the interests of management accountants driving business performance in the areas of decision support, planning, and risk and control. While our advocacy role for management accountants spans companies and public sector organizations of all sizes and types, we have thousands of members who play key roles in smaller publicly listed U.S. companies. The IMA is sensitive to their unique needs and issues and has always believed that smaller companies are the lifeblood of the entrepreneurial engine that helps drive the U.S. economy.

Although the Exposure Draft of the Final Report of the Advisory Committee on Smaller Public Companies ("the Advisory Committee") deals with a range of issues relating to microcap and smaller public companies, our comments focus only on part 3, which calls for exemptive relief for smaller public companies from the requirements imposed by Section 404 of the Sarbanes-Oxley Act of 2002 (SOX).

To meet the needs of our members for timely support on major issues impacting the management accounting profession, the IMA has invested significant time and resources over the past two years studying, researching, and providing training on SOX and the related SEC and PCAOB regulations. As part of our efforts in this area, we recently commissioned a research study that focuses on identifying and analyzing the root causes of the massive and unintended negative consequences produced by SOX Sections 302 and 404. The research results will be available in late April.

After very careful study and serious consideration of the underlying intent of the Sarbanes-Oxley Act of 2002, our conclusion is that **we are not supportive of scaled exemptions from SOX Section 404 for smaller public companies**. Having said that, **we are very supportive of major changes to the current Section 302 and 404 implementation guidance for management and external auditors – guidance we believe has produced massive unintended consequences that smaller public companies can ill afford.** It is important to note that, although the Advisory Committee analysis implies that larger companies can afford and absorb the high costs and negative consequences currently being produced by SOX regulations, we believe that costs that do not produce commensurate overall benefits to society should not be imposed on *any* public company.

With all due respect to the Advisory Committee's recommendations asking for complete or partial exemptive relief from the requirements imposed by Section 404, we believe the Committee's recommendations have the very real potential of creating a multi-tier control governance and audit opinion reliability. In other words, the companies that comply with the requirements of Section 404 will be perceived by the capital markets to have better control systems and, by extension, more reliable financial statements than the exempted companies. There is “more than a remote likelihood” that such a “multi-tier” assurance system would, in fact, end up harming smaller public companies through higher cost of capital, more restrictive debt covenants by creditors, and lower debt ratings than the short-term benefits that would flow from scaled exemptions from Section 404.

We concur with the position taken by former SEC Chairman Arthur Levitt (also Chairman of the first White House Conference on Small Business), who framed a key point very succinctly in a January 27, 2006, *Wall Street Journal* editorial:

*The debate until now has centered on who should be exempted, not on how to ensure that companies have the internal controls needed to prepare reliable financial statements. This focus is unproductive since it is clear from a reading of SOX that Congress wanted all public companies to assess internal controls and have an outside auditor test them****. Instead of defying Congress and provoking costly litigation, we need to work within the law to find ways to make compliance easier and less expensive for small business****.*

The IMA is committed to taking a leadership role in helping to develop a truly risk-based and management-centric risk and control assessment approach that companies of all sizes can use to cost effectively comply with the “spirit” of SOX outlined in Sections 302 and 404.

Although we do not support exemptive relief, it is important to note that we *do* understand the reality of the current situation and the reasons that have led the Advisory Committee to call for Section 404 exemptive relief for smaller public companies. Any unjustified financial burden imposed by inappropriate regulation has the potential to compromise U.S. global competitiveness, with small companies being disproportionately impacted. Thus, “in spirit,” we join with the Advisory Committee in raising the voice that “implementation mishaps” flowing from current SEC regulations and PCAOB guidance must be addressed and resolved as quickly as humanly possible.

THE NEED FOR PRACTICAL MANAGEMENT-CENTRIC ASSESSMENT GUIDANCE

Our analysis of the Advisory Committee’s Exposure Draft indicates that one of the major reasons the Committee is recommending exemptive relief is due to the “lack of practical management-centric assessment guidance.” The following statements from the SEC Advisory Committee’s Exposure Draft capture this frustration again and again:

”**Unless and until a framework for assessing control over financial reporting** for microcap companies is developed that recognizes the characteristics and needs of those companies...”

“**Unless and until a framework for assessing control over financial reporting** for smallcap companies that recognizes the characteristics and needs of those companies ……”

Our own, soon-to-be released SOX research study confirms the SEC Advisory Committee’s core conclusion that authoritative guidance and training for companies on how to practically and cost effectively assess and report on the state of internal control over financial reporting is currently lacking. **We believe that, rather than avoid this issue, the focus of corrective actions to the current SOX regime should be on addressing this core root cause “head-on.” The absence of practical “top-down/risk-based” assessment guidance for management is the real root cause that is at the heart of the massive and unintended consequences currently impacting companies of all sizes.**

Realizing that these changes will take time, we recommend that application of Section 404 to smaller companies commence one year following the acceptance by the SEC of new, more risk-based/management-centric assessment guidance.

In the interim, the IMA has been actively involved in “changing the vector” by pursuing various initiatives to enhance the capability of management to assess and report on the state of risk and control. We provide below a high-level summary of these initiatives and would welcome the opportunity to meet with the Advisory Committee to discuss them further.

WHAT WE ARE DOING

To date we have:

1. Raised concerns with the other members of the COSO Board regarding the capability of the COSO 1992 control model as an effective SOX assessment framework. Although in 1992 the COSO model was an important step forward, we are concerned about its applicability in providing registrants sufficient guidance in conducting cost-effective risk and control assessments to comply with the underlying spirit of Sections 302 and 404. Numerous discussions with company practitioners and auditors alike (including our preliminary research study soon to be released) revealed to us that the 1992 COSO Integrated Control Framework does not provide appropriate guidance for management to help them complete the type of practical “TOP-DOWN/RISK-BASED” control assessments called for in the May 16, 2005, SEC Staff Statement on Management’s Report on Internal Control Over Financial Reporting.

2. Confirmed through empirical research that, due to the absence of appropriate risk and control assessment guidance for management, registrants have been forced to rely upon the PCAOB Auditing Standard No. 2 as the primary source of guidance to tackle the considerable task of formally assessing and reporting on their control effectiveness. We believe that the highly granular “audit- and control-centric” assessment approach prescribed in PCAOB AS 2 has been a major cause of the massive costs and business disruptions that the Advisory Committee seeks to exempt smaller public companies from. The IMA believes that when the SEC creates practical and appropriate management-centric risk and control assessment guidance for use in complying with SOX Sections 302 and 404, AS 2 should be redrafted solely as an auditing standard that prescribes how auditors should assess whether management has completed their assessment in accordance with the new guidance. AS 2 has, by default, been the risk and control assessment standard public companies have been forced to use as primary guidance for SOX control assessments to date.

3. Proposed to the other members of the COSO Board, the SEC, and the PCAOB for comment a practical and management-centric risk and control assessment implementation framework. The proposed implementation framework is called “Collaborative Assurance and Risk Design,” and the IMA is in the process of creating an advisory board to guide its development and deployment. We believe that a management-centric assessment framework must focus on the identification and mitigation of real and plausible risks underlying the various accounting processes within an organization (including anti-fraud controls and the process used by management to create financial statements and disclosures for the capital markets). Our focus in developing this new risk and control assessment framework is to provide practical support for the type of TOP-DOWN/RISK-BASED assessment called for by the SEC.

4. Developed and launched training to help practitioners implement TOP-DOWN/RISK-BASED SOX control assessment that is aligned with the SEC May 16, 2005, directives on management reporting on internal control.

NEXT STEPS

The IMA leadership would be pleased to meet with the Advisory Committee to answer any questions on the points raised in this letter and provide more details on the research we have under way. We are committed to providing all assistance and resources we have available to address the root causes of the problems that the Advisory Committee seeks to address. The IMA passionately believes that addressing and aggressively solving the true root-cause issues underlying SOX compliance will provide maximum benefits to the U.S. economy, corporations, and shareholders.

Yours sincerely,

Paul A. Sharman, ACMA
President & CEO
Institute of Management Accountants

Jeffrey Thomson
Vice President - Research and Applications Development
Institute of Management Accountants
COSO Board Member

10 PARAGON DRIVE • MONTVALE, NJ • TEL: 800-638-4427 • TEL: 201-573-9000 • FAX: 201-474-1600 •
www.imanet.org