

October 31, 2005

PricewaterhouseCoopers LLP
400 Campus Drive
P. O. Box 988
Florham Park NJ 07932
Telephone (973) 236 4000
Facsimile (973) 236 5000

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington DC 20549-9303

RE: File Number S7-06-03

Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports of Companies That Are Not Accelerated Filers

Dear Mr. Katz:

We appreciate the opportunity to respond to the Commission's request for comments on certain issues regarding the application of Section 404 of the Sarbanes-Oxley Act of 2002 (the "Act") to smaller companies. In responding to your questions, we draw your attention to our letter submitted to you dated April 1, 2005 as it outlines our reasons for our support of the Act, which are summarized below:

- We believe the Act helps (i) to lower the inherent risk in the US capital markets and (ii) to enhance investor confidence, thus resulting in a more efficient allocation of capital among market participants.
- We acknowledge the cost of complying with the Act and related requirements established by the Public Company Accounting Oversight Board's ("PCAOB") Auditing Standard No. 2 ("AS 2") are significant, and should be allowed the time needed to prove that the benefits to investors can be realized.
- We believe investors benefit from the consequence that executive and operating management have a deeper appreciation for their responsibilities over internal controls over financial reporting.

We also acknowledged that we expect the future costs incurred related to complying with the Act are likely to be much lower.

We have provided our answers to certain of the questions posed by the Commission and respectfully submit them for consideration.

- **Should there be a different set of internal control over financial reporting requirements that applies to smaller companies than applies to larger companies? Would it be appropriate to apply a different set of substantive requirements to non-accelerated filers, or for management of non-accelerated filers to make a different kind of assessment?**

As stipulated above, we believe that the Act has provided a number of key benefits to the US capital markets. We also believe that uniform application of the Act to all companies who wish to access public capital markets best serves investors. Consistent treatment for all companies creates a common environment of transparency and reliability for investors which forms a common platform upon which an investor is more efficiently able to assess expectations of a company's future prospects.

However, we also acknowledge the concerns expressed by some that the cost of complying with the provisions of the Act for "very small companies" may be disproportionately high so as to raise fundamental questions about capital formation in this sector. It is our view that this concern arises, in substantial part, because it is envisioned that the cost of complying with the Act and AS 2 represents a consequential cost, even when all possible efficiencies in application are achieved. This cost may be disproportionately high to "very small companies" as compared to other companies.

Moreover, we acknowledge that "very small companies" represent one of the lifebloods of the US capital markets and that maintaining a healthy environment for capital formation is an important consideration for policy makers when balancing the need to achieve the benefits desired by the Act with the costs of compliance.

We acknowledge that some observers are petitioning policy makers to consider providing an exemption for small companies from compliance with Section 404. We would not object if such an exemption were provided for "very small companies" as articulated above. We believe, however, that the decision to avail themselves of the exemption offered should be subject to audit committee and/or shareholder approval.

- **Would a public float threshold that is higher or lower than the \$75 million that we use to distinguish accelerated filers from non-accelerated filers be more appropriate for this purpose? If so, what should the threshold be and why? Would it be better to use a test other than public float for this purpose, such as annual revenues, number of segments or number of locations or operations? If so, why?**

Whether the \$75 million threshold consistently identifies "very small companies" is unclear and may deserve further study. However, we also acknowledge that the market capitalization represented by companies with less than \$75 million in public float represents a very small percentage of US equity capital¹. While we would prefer to limit any exemption only to very small companies as the term is used above, we acknowledge that using the same threshold to distinguish accelerated filers from non-accelerated filers may be an appropriate balance between the needs of the investors and the cost of compliance.

We believe that a measure based on public float is appropriate for regulations intended for the benefit of investors, including those related to the timing and content of public filings. We understand that the use of public float alone may unfairly burden some companies who share the characteristic problems of limited sophistication and resource constraints, but we believe that there will be outliers in any threshold selected and that public float is a reasonable proxy for an issuer's level of development.

- **Should the independent auditor attestation requirement be different for smaller public companies? If so, how should the requirements differ?**

While understanding that some very small companies may be offered an exemption from Section 404, we believe that all companies subject to the internal control over financial reporting requirements should be subject to the same independent auditor attestation requirements.

¹ See Office of Economic Analysis statistics as quoted in *Revisions to Accelerated Filer Definition and Accelerated Deadlines for Filing Periodic Reports*, Release No. 33-8617, Section V.B.

- **Should the same standard for auditing internal control over financial reporting apply to auditors of all public companies, or should there be different standards based on the size of the public company whose internal control is being audited? If the latter, how should the standards differ?**

We believe that the same standard for auditing internal control over financial reporting should be applied to all companies, regardless of size.

- The fundamental underpinnings of Auditing Standard No. 2, *An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements* (AS 2), include the concepts of materiality, reasonable assurance, and principal level of evidence. We believe that these underpinnings apply equally to audits of internal control at a large or small company.

AS 2, coupled with the interpretive guidance issued by the PCAOB and the SEC, allows auditors the necessary flexibility to design a risk-based approach to appropriately address the risks associated with a particular company regardless of the company's size.

- We believe that suggestions that an auditor could reduce or eliminate independent testing are contrary to the intent of Section 404.

For example, we believe that the auditor's own work should be the principal evidence for the auditor's opinion regardless of the size of the company. An auditor's leverage of the use of the work of others is equally appropriate for small companies when determining how the auditor will obtain their audit evidence over design and operating effectiveness. We believe that the determination of the controls for which the auditor can rely on management's testing should be based on the nature of the control, the competence and objectivity of those performing the work, and the quality and effectiveness of the work performed regardless of the company's size. The results of this analysis will vary from company to company as is appropriate for an approach that is tailored to individual circumstances.

- A different auditing standard for audits of internal control over financial reporting for larger versus smaller companies may create confusion among financial statement users as to the conclusions that should be drawn on the effectiveness of internal control over financial reporting. We believe this would increase an already considerable expectation gap as to the amount of comfort provided by the auditor's attestation.



- **How can we best assure that the costs of the internal control over financial reporting requirements imposed on smaller public companies are commensurate with the benefits?**

We reference our April 1, 2005 letter to you which describes the benefits to key stakeholders in the capital markets that we believe result from the Act, including, among others, increased reliability and transparency of financial statements, enhanced business processes, and reduction of risk. We recognize that achieving the desired benefits of the Act requires all companies to incur a certain level of investment which is relatively easily quantifiable. We also recognize that the benefits described above are difficult to quantify, but we believe they form the foundation to provide reliable and objective information for investors in the US capital markets. We continue to support consistent application of the Act to all companies (acknowledging the possible relief for very small companies discussed above) and believe that cost reductions can be achieved through the development of efficiencies in the application of the existing framework.

* * * * *

We appreciate the opportunity to express our views and would be pleased to discuss our comments or answer any questions. Please do not hesitate to contact Vincent P. Colman (973-236-5390) or Raymond Beier (973-236-7440) regarding our submission.

Sincerely,

PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP