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Memorandum to the Securities and Exchange Commission

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Subject: File Number S7-24-06, Management's Report on Internal Control Over Financial Reporting

Given the very real burden imposed by Section 404 of the Sarbanes-Oxley Act on American companies and the real and perceived impact of that law on the international competitiveness of American financial markets, the proposed regulations are definitely a step in the right direction. However, while this proposal may be what is achievable today, additional changes will be required in the future, and this should be regarded as merely a first step towards more fundamental reform.

For that reason, the Commission should institute regular periodic review of regulations required by Section 404 as well as that section's impact on financial competitiveness to determine if additional regulatory changes are necessary. This review should take place at intervals no longer than every two years. In addition, that review should also determine if statutory changes should be recommended to Congress. Sarbanes-Oxley's impact is likely to grow as the rest of the world financial markets change their regulatory regimes in order to better compete with American markets, and a mechanism should be in place to review all Sarbanes-Oxley-related regulations.

At the same time, even the best regulatory changes will not reduce regulatory burdens unless auditors and management actually change their practices. Given the current climate where both fear lawsuits challenging even the most innocent decisions, real reduction in the regulatory burden that is imposed by Section 404 of Sarbanes-Oxley may require a waiver that gives auditors some level of protection against liability. As a result, the Commission should consider in consultation with the PCAOB whether such a waiver would be desirable, and if so, formally recommend that Congress consider legislation on that subject.

Finally, current SEC regulations on Section 404 go well beyond the direct intent of Congress in that they require a company's internal financial controls to include controls for the safeguarding of assets. While other laws do require internal controls that safeguard assets, those controls did not have to be certified by an outside auditor. It is very hard to imagine a case where the theft or loss of assets would be so great as to require reporting in a financial statement. Given the concern about the burden imposed by Section 404, the Commission could take a significant step in reducing that burden by withdrawing the portion of its regulations dealing with the safeguarding of assets.