

CAQ Alert #2010-28 – May 19, 2010

DEAR CENTER MEMBERS

[Absent a Legislative Exemption, Sarbanes-Oxley Section 404\(b\) Remains Effective June 15, 2010](#)

As outlined by the SEC (or Commission) in October 2009, non-accelerated filers with fiscal years ending on or after June 15, 2010 will be required to have an audit of internal control over financial reporting in accordance with [Section 404\(b\) of the Sarbanes-Oxley Act of 2002](#). As June 15, 2010 rapidly approaches, CAQ member firms continue to raise questions regarding the status of 404(b) compliance. Specifically, members have inquired as to whether recent legislative activity will exempt non-accelerated filers from having to comply with Section 404(b) and if that legislative activity is unresolved by the effective date, members have questioned whether the SEC plans to issue another deferral.

This alert includes a summary of recent SEC actions and legislative activity related to Section 404(b) that has occurred to date and also discusses what will be required absent legislative exemption by June 15, 2010.

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It is important to note that as of the writing of this alert, there has been NO deferral of the June 15, 2010 effective date for non-accelerated filers. The CAQ will continue to monitor legislative activity related to 404(b) as it transpires and plans to update our members accordingly. Also, future CAQ communications will provide our members with perspectives on matters to consider in complying with the attestation requirements under Section 404(b) for the first time, including a list of resources to assist auditors as they embark on this process.

Legislative Activity

The U.S. House of Representatives passed a comprehensive regulatory reform bill – the “Wall Street Reform and Consumer Protection Act” (H.R. 4173) - in December 2009. The U.S. Senate continues to debate aspects of its regulatory reform bill. In mid-March 2010, following four months of negotiations with Banking Committee Republicans, Sen. Dodd introduced the “Restoring American Financial Stability Act” (S. 3217), without Republican support. The bill was reported to the Senate floor on March 22nd. Following three unsuccessful votes to end a Republican filibuster, debate on S. 3217 began on April 29th.

The House bill includes a provision to permanently exempt public companies with market capitalizations below \$75 million from complying with Section 404(b) of the Sarbanes-Oxley Act. The bill also would require the SEC to “conduct a study to determine how the Commission could reduce the burden of complying with section 404(b) of the Sarbanes-Oxley Act of 2002 for companies whose market capitalization is between \$75 million and \$250 million for the relevant reporting period while maintaining investor protections for such companies.” A separate provision would require the Government Accountability Office to conduct a study to determine: the efficacy of the SEC’s measures to limit smaller issuers’ 404(b) compliance costs; how to “reduce the burden of” 404(b) compliance for companies with market capitalizations of less than \$250 million; and whether reducing the compliance burden or a complete compliance exemption for companies with market capitalizations of less than \$250 million would encourage companies to list on U.S. Exchanges in their initial public offerings.

The Senate bill currently includes no 404(b) exemption, however, two amendments exempting companies from Section 404(b) compliance have been filed. An amendment filed by Sen. David Vitter (R-La.) would exempt companies with market capitalizations below \$75 million. It would also require

the SEC and Comptroller General to jointly study “how the Commission could reduce the burden of complying with section 404(b) of the Sarbanes-Oxley Act of 2002 for companies whose market capitalization is between \$75,000,000 and \$250,000,000 for the relevant reporting period, while maintaining investor protections for such companies.” An amendment co-sponsored by Sens. Kay Bailey Hutchison (R-Texas) and Mary Landrieu (D-La.) would grant a permanent 404(b) exemption to companies with market capitalizations of less than \$150 million—which would include some companies already complying with 404(b). It also would require the SEC to conduct a study to determine ways to “reduce the burden of complying with” 404(b) for companies with market capitalizations between \$150 million and \$700 million. It should be noted that from a process perspective, if/when a bill is approved by the Senate, it must then be reconciled with the bill currently approved in the House, subjected again to approval by Congress, and then ultimately signed into law by the President before any provisions come into effect.

Status of Section 404(b) Effective Date for Non-Accelerated Filers

In October of 2009, the SEC [announced](#) an additional six-month deferral for non-accelerated filers from complying with the provisions of Section 404(b) of the Sarbanes-Oxley Act of 2002. In the press release announcing the deferral the SEC indicated that the six-month deferral was granted as a result of the late issuance of the SEC’s [cost-benefit study](#) conducted by its Office of Economic Analysis. Under this extension, non-accelerated filers (smallest public companies with a public float below \$75 million) are currently required to provide the auditor attestation reports in their annual reports for fiscal years ending on or after June 15, 2010. The expiration date previously had been for fiscal years ending on or after December 15, 2009.

With regard to the deferral, SEC Chairman Mary Schapiro stated, “Since there will be no further Commission extensions, it is important for all public companies and their auditors to act with deliberate speed to move toward full Section 404 compliance.”

How is Section 404(b) Compliance Affected Without Legislative Exemption for Non-Accelerated Filers by June 15, 2010?

Without a legislative exemption, non-accelerated filers will be required to comply with Section 404(b) beginning with the annual reports for fiscal years ending on or after June 15th. It is unclear 1) whether the Senate and House will agree on a bill that contains a permanent exemption of Section 404(b) for non-accelerated filers; 2) whether such a bill will ultimately be approved by the President; and 3) whether both 1) and 2) will occur before the SEC filing date for non-accelerated filers with fiscal years ending on or after June 15, 2010 (approximately September 15th for companies with a June 15th year-end).

At the PCAOB’s April 2010 Standing Advisory Group meeting, Wayne Carnall, Chief Accountant of the SEC’s Division of Corporation Finance, was asked about the status of Section 404(b) and whether the Commission had intentions of issuing another deferral. Mr. Carnall responded by stating that Chairman Schapiro has gone on record stating that the October 2009 deferral was the final deferral for non-accelerated filers.

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