

Summer 2006

*To Our Clients  
and Friends*

## Sarbanes-Oxley Compliance Relief for Certain Non-US Companies<sup>1</sup>

On August 9, 2006, the United States Securities and Exchange Commission ("SEC") published proposed and final rules which together would:

- Extend certain deadlines for compliance with the internal control reporting requirements of Section 404 of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") for certain non-U.S. companies;
- Split the compliance deadlines under Section 404 of Sarbanes-Oxley ("Section 404") for the management report on internal controls over financial reporting and the related auditors' report; and
- Provide additional relief from Section 404 compliance for newly public companies.

Under the proposed rule, all newly public companies would benefit from a one year deferral for Section 404 compliance, and certain non-U.S. companies would benefit from new Section 404 compliance deferrals. The deadlines for Section 404 compliance under the *proposed* (in italics) and **final** (in bold) rules as they stand at present (for annual reports filed for fiscal years ending *on or after the specified dates*) are as follows:

<b>Issuer</b>	<b>Management Report Deadline</b> (Reg. S-K Item 308(a))	<b>Auditors' Attestation Report Deadline</b> (Reg. S-K Item 308(b))
Non-U.S. Company Non-Accelerated Filers <sup>2</sup>	<i>December 15, 2007</i> <i>(proposed)</i>	<i>December 15, 2008</i> <i>(proposed)</i>
Non-U.S. Company Accelerated Filers (not Large Accelerated Filers) <sup>3</sup>	<b>July 15, 2006</b> <b>(final)</b>	<b>July 15, 2007</b> <b>(final)</b>
Non-U.S. Company Large Accelerated Filers <sup>4</sup>	<b>July 15, 2006</b> <b>(final)</b>	<b>July 15, 2006</b> <b>(final)</b>
Newly Public Companies	<i>2nd Annual Report filed with SEC (proposed)</i>	<i>2nd Annual Report filed with SEC (proposed)</i>

Until filing an annual report that includes a report by management on the internal controls over financial reporting, a Non-Accelerated Filer will be allowed to omit from the annual CEO and CFO certifications references to the certifying officers' responsibility for designing, establishing and maintaining internal controls over financial reporting for the issuer. The SEC has also proposed that management reports for fiscal years not subject to auditors' attestation would be deemed "furnished" to the SEC rather than "filed." The intent of this proposal is to avoid the potential of the auditors' attestation report in the second year of compliance calling into question the management report on the internal controls over financial reporting in the first year of compliance.

## **SEC Responds to Concerns of Small Issuers**

The SEC and the Public Company Accounting Oversight Board ("PCAOB") have acknowledged the unique issues that smaller companies face with the internal control reporting requirements imposed by Section 404 and have recently undertaken several initiatives to provide guidance to these issuers. The extension of the Section 404 compliance deadlines is intended to allow these issuers the benefit of such guidance prior to the implementation of internal control procedures over financial reporting and the assessment of such procedures. Approximately 61% of all non-U.S. companies are small issuers within the SEC's rules and will receive some relief from these new compliance deadlines.

The split of the management report deadline and the auditor attestation deadline for Non-Accelerated Filers and Accelerated Filers (other than Large Accelerated Filers) is in direct response to comments previously received by the SEC. Certain commenters have noted that the initial reporting compliance costs imposed by Section 404 are disproportionately high for smaller companies and that the auditors' fees are a large part of those costs. In addition, it is believed that first year costs will be higher for all filers than subsequent years due to the non-recurring initial set-up costs. The deferral of the auditors' attestation until the second year of compliance is intended to defer the increased auditors' costs to the second year of compliance at which time their effect would be somewhat offset by the absence of the costs associated with initial compliance. The net effect would be less of a compliance cost "spike" to the issuer in any given year.

## **Transitional Relief for Newly Public Companies**

Under current rules, both U.S. and non-U.S. companies would be required to comply with the internal control reporting requirements imposed by Section 404 as of the end of the first year in which they become a public company. In recognition of the burdens that preparation of the first annual report imposes on newly public companies, the SEC has concluded that the addition of the management report and auditors' attestation on the effectiveness of internal controls over financial reporting to the first annual report process might prove an undue burden on newly public companies. The SEC also expressed a concern that requiring such reports in the first annual report of a newly public company might deter certain issuers, including non-U.S. companies, from accessing the U.S. capital markets. In response to these concerns, the SEC has proposed that a new public company would not need to comply with the management report and auditors' attestation for internal controls over financial reporting until the filing of its second annual report with the SEC.

## Sarbanes-Oxley Compliance Relief for Certain Non-US Companies

Should you have a question on the subject, please contact Herman H. Raspé at 212.336.2301 (hhraspe@pbwt.com), or Karen McCarthy at 212.336.2529 (kmmccarthy@pbwt.com).

### Endnotes

- <sup>1</sup> For purposes of this Client Alert, the term "non-U.S. company" is intended to mean a "Foreign Private Issuer" (as such term is defined in the rules adopted by the SEC under the United States Securities Exchange Act of 1934 ("Exchange Act")).
- <sup>2</sup> A Non-Accelerated Filer is an issuer that does not come within the definitions of Accelerated Filer or Large Accelerated Filer in Rule 12b-2 under the Exchange Act as summarized below.
- <sup>3</sup> An Accelerated Filer as defined in Rule 12b-2 under the Exchange Act is an issuer that (i) has an aggregate worldwide market value of its common equity securities of \$75 million or more but less than \$700 million held by non-affiliates as of the end of the most recently completed second fiscal quarter, (ii) has been subject to the periodic reporting requirements of the Exchange Act for at least twelve (12) months, (iii) has filed at least one annual report, and (iv) is not eligible to utilize small business issuer forms for its quarterly and annual reports.
- <sup>4</sup> A Large Accelerated Filer as defined in Rule 12b-2 under the Exchange Act is an issuer that (i) has an aggregate worldwide market value of its common equity securities of \$700 million or more held by non-affiliates as of the end of the most recently completed second fiscal quarter, (ii) has been subject to the periodic reporting requirements of the Exchange Act for at least twelve (12) months, (iii) has filed at least one annual report, and (iv) is not eligible to utilize small business issuer forms for its quarterly and annual reports.

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