

Securities Law Update

March 2005

SEC Further Delays Section 404 Reporting Requirements for Non-Accelerated Filers and Foreign Private Issuers

The SEC has extended the compliance dates for rules that require a company to include in its annual reports a report by management on the company's internal control over financial reporting and an accompanying auditor's report. These compliance dates have been extended previously, most recently in November 2004.

Under the latest extension, companies that are not required to file periodic reports on an accelerated basis (non-accelerated filers), and foreign private issuers that file on Form 20-F or 40-F, must begin to comply with the internal control over financial reporting requirements, which were mandated by Section 404 of the Sarbanes-Oxley Act, for the first fiscal year ended on or after July 15, 2006. For calendar year companies, the extension means that no Section 404 reports will be due until early 2007.

As readers probably know, an accelerated filer is an issuer that meets the following conditions:

- § The aggregate market value of the voting and non-voting common equity held by non-affiliates of the issuer is \$ 75 million or more;
- § The issuer has been subject to the requirements of Section 13(a) or 15(d) of the Securities Act for a period of at least 12 calendar months;
- § The issuer has filed at least one annual report under Section 13(a) or 15(d) of the Act; and
- **§** The issuer is not eligible to use Forms 10-KSB or 10-QSB for its annual and quarterly reports.

The extended compliance period for non-accelerated filers and foreign private issuers also applies to the certifications that refer to the certifying officers' responsibility for establishing and maintaining internal control over financial reporting for the company.

The SEC stated that the extension should make implementation of the internal control reporting requirements more effective for non-accelerated filers and foreign private issuers. This will benefit investors and improve confidence in the reliability of the disclosure made by these companies about their internal control over financial reporting.

The SEC emphasized, though, that this extension should not be viewed as a basis for smaller companies and foreign private issuers to slow down or delay their Section 404 compliance efforts. Smaller companies or foreign private issuers may find that they need all the time available, including the time afforded by this extension, to comply fully with the internal control reporting requirements.

A Ray of Hope for Less Rigorous Standards for Smaller Companies?

The SEC's announcement of the extension contained a ray of hope for those who believe that smaller companies should be subject to less rigorous (some would say less burdensome) regulation of their internal control requirements. The Commission noted that it has established an SEC Advisory Committee on Smaller Public Companies "to assist the SEC in evaluating the current securities regulatory system relating to smaller public companies." In addition, the release noted that the Committee of Sponsoring Organizations, or COSO, a voluntary private sector organization dedicated to improving the quality of financial reporting, "has established a task force to develop new guidance for smaller companies that it intends to publish this summer."

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