

SEC Approves New Guidance for Compliance with Section 404 of Sarbanes-Oxley



We thought you should know:

As expected, the Securities and Exchange Commission (SEC) voted on May 23, 2007, to adopt final guidance for management on evaluating and assessing internal control over financial reporting as required by Section 404 of Sarbanes-Oxley. The SEC also said it will not delay implementation for non-accelerated filers, which means those companies will comply with the management reporting provisions by their fiscal year ending after December 15, 2007 and the auditor attestation requirement a year later, as planned.

See the complete press release from SEC below.

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FOR IMMEDIATE RELEASE

2007-101

Washington, D.C., May 23, 2007 — The Securities and Exchange Commission today unanimously approved interpretive guidance to help public companies strengthen their internal control over financial reporting while reducing unnecessary costs, particularly at smaller companies. The new guidance will enhance compliance under Section 404 of the Sarbanes-Oxley Act of 2002 by focusing company management on the internal controls that best protect against the risk of a material financial misstatement.

“Congress never intended that the 404 process should become inflexible, burdensome, and wasteful. The objective of Section 404 is to provide meaningful disclosure to investors about the effectiveness of a company’s internal controls systems, without creating unnecessary compliance burdens or wasting shareholder resources,” said SEC Chairman Christopher Cox. “With the Commission’s new interpretive guidance for management on the evaluation and assessment of its internal controls over financial reporting, companies of all sizes will be able to scale and tailor their evaluation procedures according to the facts and circumstances. And investors will benefit from reduced compliance costs.”

“Our guidance enables companies of all sizes to focus on what truly matters to the integrity of the financial statements – risk and materiality,” said Conrad Hewitt, Chief Accountant. “Providing management with its own guidance for



evaluating internal control over financial reporting will ensure an appropriate balance between management's evaluation process and the audit process. While the guidance is intended to help public companies of all sizes, smaller companies, which will begin complying with Section 404 this year, should benefit from its scalability and flexibility. We have also worked closely with the PCAOB to better align our interpretative guidance and the PCAOB's proposed auditing standard, which the PCAOB will consider for adoption tomorrow."

"As investors have made clear, Section 404 serves a critically important role in fostering the reliability of financial statements upon which investors and our markets depend. The guidance issued today achieves a significant step in the roadmap the Commission laid out a year ago for improving the implementation of Section 404 for public companies of all sizes and their investors alike," said John W. White, Director of the SEC's Division of Corporation Finance. "The Commission and its staff have been focused on improving Section 404 implementation for some time, and our efforts have been considerably aided by the public comment process and helpful insights and suggestions that various interested persons have provided us. The Commission's interpretive guidance should reduce uncertainty about what constitutes a reasonable approach to management's evaluation while maintaining flexibility for companies that have already developed their own assessment procedures and tools that serve the company and its investors well. Companies will be able to continue using their existing procedures if they choose, provided of course that those meet the standards of Section 404 and our rules."

The Commission also approved rule amendments providing that a company that performs an evaluation of internal control in accordance with the interpretive guidance satisfies the annual evaluation required by Exchange Act Rules 13a-15 and 15d-15. The Commission also amended its rules to define the term "material weakness" as "a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis." The Commission also voted to revise the requirements regarding the auditor's attestation report on the effectiveness of internal control over financial reporting to more clearly convey that the auditor is not evaluating management's evaluation process but is opining directly on internal control over financial reporting.

The effective date of the interpretive guidance and adopted rules will be 30 days from their publication in the Federal Register. The full text of the interpretive guidance and rules will be posted to the SEC Web site as soon as possible. The new auditing standard will be subject to Commission approval in the coming months after its adoption by the PCAOB and, if approved, is expected to be effective no later than for calendar year 2007 audits, with early adoption encouraged.

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For more information, contact:

Larry Hessney
office: 585.256.2090 x107
cell: 585.721.1508
larry.hessney@freedmaxick.com