



IASBDA

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The International Association of Small broker-dealers and advisers [www.IASBDA.COM](http://www.IASBDA.COM) submits the following comments on the SOX Roundtable. The SEC'S Small Business Committee recommends that small firms be relieved of their SOX burdens and many including former SEC Chairman Levitt and FED Chairman Volcker(The Chairmen) have already written in opposition claiming that the small firms are more problematic.The Committee,Commission and PCAOB(The Regulators) need to address this argument in a more systematic way by analyzing what is problematic. The Chairmen contend that there are more restatements(75%) among companies with less than \$500 in revenue but the committee recommends exempting those with less than \$125 million in revenue. Interestingly the chairmen do not recommend extending SOX to the least regulated entities,the Pink Sheets. The real issue however is losses to shareholders and there is strong evidence that this has been more true for the large issuers like Enron,Worldcom,Adelphia,Quest,Global Crossing and Refco. Thus while it is self evident and admitted that small firms have higher proportionate compliance costs, it is not self evident that their shareholders have suffered more even if there are more restatements because those restatements may well be honest mistakes. Moreover the demise of many small firms for business reasons should not be confused with fraudulent accounting.SOX was not intended to fix poor business practices but rather fraudulent business practices.

One commentator explains "Sarbanes-Oxley's focus on internal controls -- the systems put in place to make sure factual financial and other important information actually reaches top management -- has led to an environment of second-guessing by auditors, where even a minor accounting error can mushroom into a wholesale investigation of a company's accounting procedures. The law put the onus on chief executives to certify they have taken all reasonable efforts to make sure that the numbers are correct and that their companies are fraud-free. The result, experts say, is a rush to get every possible error, no matter how small, identified and disclosed.

*"I think what [Sarbanes-Oxley] did, it created an environment where companies aren't allowed to make honest mistakes," said Colleen Sayther Cunningham, president of Financial Executives International, a trade group of 15,000 chief financial officers and other financial executives. "You're seeing companies wounded by errors that in the past wouldn't have required a restatement but would have been fixed going forward." Wash Post January 30 2006.*

The SEC'S former Chief Accountant Donald Nicolaison noted that not all material weaknesses will be viewed with equal significance

*"some material weaknesses may have a greater or lesser impact on an investor's decision-making process. In many cases, this decision will likely be influenced by the fullness of management's disclosure, the underlying causes of the material weakness, and management's actions to address the material weakness. This is intended to be an open process whereby investors can evaluate both the weakness as well as management's actions to improve controls." speech at 11th Annual Midwestern Financial Reporting Symposium*

The Regulators have to resolve this debate through an independent study of small firm accounting enforcement actions and should arrange for one to be done by a University. At the very least the accounting enforcement actions against small firms should be publicly considered as there are very few of them. It should not impose the costs of SOX on small firms until it has proof that the costs justify the remedy. Alternatively it could do a pilot study of the OTCBB to see how many shareholders are harmed by accounting irregularities over a short period of time. The argument for not imposing the same regulatory burden on small firms is one of proportionality. The small firms are hurt more by the auditing costs and may not present the same danger to shareholders. The small firms that trade on the OTCBB need an alternative to individual audits. One solution might be allowing them to share the auditing costs that the bigger firms can individually absorb. They might therefore be allowed to form an association that would provide auditors whose costs were shared by numerous small firms under the oversight of the PCOAB. Firms choosing not to join would be bound by SOX. Such an association might also provide the accounting assistance suggested by both the Chairman and the Committee.. The Commission under its SOX authority could allow an association of small issuers to pool their resources into an auditing coop overseen by the PCAOB. The coop would hire a force of auditors to perform the internal controls audit under the PCAOB. The association would be supported by yearly fees based on revenue.. The Association might also receive

additional funding from educational seminars and small business supporters and perhaps even NASDAQ . It would to some degree replace the extra SEC small business staff that has been suggested by the Chairmen. These association auditors would gain expertise over time in internal controls and become more efficient and more effective and as the companies grew they would move on to a regular SOX audit. Finally whatever is decided should meet the fundamental principle of medical ethics;"First do no harm."

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