

**Written Statement of**

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Sioux Falls, SD**

**Securities and Exchange Commission Roundtable**

**“Implementation of Internal Control Reporting Provisions”**

**April 13, 2005**

Members of the Securities and Exchange Commission,

My name is Curt Hage and I am Chairman and CEO of HF Financial Corp, and Home Federal Bank in Sioux Falls, South Dakota, and am a former Chairman of America's Community Bankers. I appreciate the opportunity to participate in the SEC's Public Roundtable on Implementation of Internal Control Reporting Provisions and welcome the opportunity to submit these written remarks.

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HF Financial Corp is a unitary thrift holding company and is publicly traded on NASDAQ. Home Federal Bank is a community bank with approximately \$850 million in assets, our company reports on a June 30 fiscal year-end and we are a non-accelerated filer for purposes of Section 404 of Sarbanes-Oxley. Nonetheless, we have recently started the substantive portion of our Section 404 implementation efforts with our staff and with our external auditors. Based on our experience, we are extremely concerned that the processes required for implementing and complying with Section 404 raise some serious dilemmas for all financial institutions.

Undoubtedly, the SEC and PCAOB have received a tremendous amount of feedback from registrants on the mounting and overwhelming costs being imposed on companies as a result of the landmark Sarbanes-Oxley Act. I would be remiss if I did not loudly echo these concerns on behalf of my own institution. The financial constraints and other problems emerging as companies struggle to comply with the new law and the associated

audit requirements threaten the ability of community banks to economically compete and continue to serve their vital role in today's financial services industry.

Banks were already heavily regulated before Sarbanes-Oxley. As a bank with over \$500 million in assets, Home Federal was already subject to the audit and attestation reporting requirements prescribed by the FDIC regulations, commonly referred to as FDICIA.

Since external auditors now have a newfound authority and directive under the Act and are acting more like bank examiners, banks are becoming significantly overwhelmed by the over-regulation. The examiners and external auditors are often duplicating efforts, and in many cases, disagreeing on some financial statement reporting or internal controls issues. These disagreements are often leaving financial institutions confused and at a loss about which "supervisory body" with which they should comply. While the banking regulators, the SEC and PCAOB will typically get involved to try and resolve discrepancies involving larger institutions, they are less likely to respond to the pleas when smaller banks have examiner / external auditor disagreements.

### **Cost-Benefits of Disclosures**

Financial institutions are both preparers and users of financial statements, and we would certainly welcome efforts to improve the accuracy and transparency of financial reporting. However, it seems highly unlikely that users of financial statements will recognize a benefit commensurate with the extraordinary costs and resource burdens associated with Section 404. There is little to suggest that a typical investor will benefit much at all from Section 404's management and auditor reports on internal controls or from a company's disclosure of a material weakness. The new auditing standards appear

to have put auditors on the defensive, creating an environment where they are now enforcing some very rigid interpretations of longstanding accounting standards, sometimes requiring restatements.

Additionally, the ambiguous definitions and low thresholds ascribed to “significant deficiencies” and “material weaknesses” appear to be confusing investors and are likely to cause disclosure of irrelevant and immaterial matters. This result would be inconsistent, if not counterintuitive, to the SEC’s recent guidance on decreasing the volume and improving the quality of financial statement disclosures. Much of the problems arising between the accounting firms and their clients surrounding Section 404 efforts have led to an amazingly high number of delayed filings, which are causing concerns that could be seriously misguided.

Managements’ and auditors’ Section 404 reports are likely to result in management gaining a better understanding of the internal controls processes, and may even highlight some weaknesses in the systems that needed to be rectified. However, these modest improvements are only efficient if they come at a reasonable cost. The weaknesses most companies appear to be disclosing are clearly not Enron-like abuses, are not likely to lead to the company failing, nor do they pose substantial risks to the company. In a successful business model, banks must assume a reasonable level of business risk, precluding excessive measures and costs that would be required to eliminate moderate risks. Sarbanes-Oxley Section 404 and PCAOB Auditing Standard 2 have effectively created a vehicle where public companies are being subject to over-compensating and costly

measures to “remove” many of the risks that were previously identified and deemed insignificant by regulators under banking laws and regulations.

Without proper oversight and controls over the related fees being imposed for Section 404 implementation and compliance, and a profound inability to adequately assess the benefit gained through Section 404 reports and disclosures, this system appears doomed to failure. Smaller public companies like Home Federal Bank are starting to wonder how many additional funds and resources can be allocated to comply with this new standard, on top of the existing bank regulatory burdens, with little confidence as to a commensurate benefit to our organization or its investors. Without some form of reasonable relief provided by the SEC and PCAOB, real and unfortunate conclusions for many community financial institutions will likely be dissolution through merger activity, or becoming private enterprises.