



November 29, 2011

The Honorable Spencer Bachus
Chairman
House Financial Services Committee
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Barney Frank
Ranking Member
House Financial Services Committee
B371A Rayburn House Office Building
Washington, DC 20515

Dear Chairman Bachus and Ranking Member Frank:

The Center for Audit Quality (CAQ) and the Council of Institutional Investors (CII) respectfully urge you to resist legislative efforts to further weaken investor protections of the Sarbanes-Oxley Act of 2002 (SOX). In particular, we hope you will stand firm in rejecting attempts to exempt even more public companies from compliance with Section 404(b) of the Act, which requires an independent audit of a company's assessment of its internal controls over financial reporting (ICFR).

It is important to note that the processes associated with attesting to a public company's internal control effectiveness are now fully integrated into the financial statement audit. As a result, the benefits of the internal control audit far outweigh the costs, which was a valid concern expressed during the early days of Section 404 implementation. Further, the original Public Company Accounting Oversight Board (PCAOB) standard that implemented auditor attestation of internal controls over financial reporting, Auditing Standard (AS) No. 2 was rescinded in 2007 and replaced by AS No. 5 to facilitate an integrated audit. In addition, the Securities and Exchange Commission (SEC) also issued useful guidance for management to assist with the implementation of Section 404 by allowing for a scalable assessment based on the complexity of the company. These steps have led to considerable cost savings, significantly alleviating past concerns about the costs associated with 404(b) compliance. Thus, we believe that the value of an external assessment of the internal control over financial reporting in promoting confidence in our markets and the capital formation process should be emphasized – and arguments that 404(b) is hindering economic growth should be scrutinized carefully.

A year ago, the Dodd-Frank Wall Street Reform and Consumer Protection Act gave permanent exemption to non-accelerated filers, i.e., issuers with a public float up to \$75M, which exempted 42% of public companies¹. The Act also mandated a study by the SEC released last April² which concluded that the existing requirements for issuers with a \$75-\$250 million public float to comply with the auditor attestation provisions of Section 404(b) should be maintained and that no new exemptions should be granted. More recently, SEC Chairman Mary Schapiro reported that the SEC has heard repeatedly from investors that they have more confidence in financial reporting when an auditor conducts an independent assessment of internal control over financial reporting. In a letter to Rep. Scott Garrett on October 4,

¹ Analysis of data from Audit Analytics database of “Tickered 34 Act Filers” as of September 27, 2011.

² Study and Recommendations on Section 404(b) of the Sarbanes-Oxley Act of 2002 For Issuers With Public Float Between \$75 and \$250 Million, U.S. Securities and Exchange Commission, <http://www.sec.gov/news/studies/2011/404bfloor-study.pdf>, April 2011.

2011, Chairman Shapiro also pointed out that the SEC's study found that companies that do not have an audit of management's assessment of internal controls over financial reporting tend to have both significantly more material weaknesses in their internal controls and more restatements of their financial statements.

The Dodd-Frank Act also called upon the Government Accountability Office (GAO) to conduct a study on the impact of Section 404(b) amendments on restatement rates, cost of capital, and investor confidence, and to submit a report within three years of the law's enactment (by no later than July 21, 2013). While we believe there currently is ample evidence against further rollbacks, we believe it would be prudent to understand the results of the GAO study before exempting more companies from Section 404(b).

Investors are increasingly troubled by the world's economic challenges. In fact, the CAQ's recent Main Street Investor Survey found that confidence in U.S. capital markets has dropped steadily since 2009 – to 61 percent this year.³ Congress should do everything in its power to enhance and regain that confidence, not undercut it. We urge you to preserve the remaining investor safeguards contained in SOX Section 404(b).

Sincerely,



Cindy Fornelli
Executive Director
Center for Audit Quality



Jeff Mahoney
General Counsel
Council of Institutional Investors

cc: Members of the House Financial Services Committee

³ Center for Audit Quality, Fifth Annual Main Street Investor Survey,
<http://www.thecaq.org/newsroom/pdfs/2011InvestorSurveySummaryHighlights.pdf>, October 2011.