

legal requirement and not a listing requirement.¹⁶³ Others believed that the exemption as proposed would not cover the unique situations in some countries where the board of auditors or similar body consists of one or more independent members of the board of directors in addition to one or more non-board members.¹⁶⁴ Without a modification, these commenters believed issuers from such jurisdictions could not satisfy the exemption because of the requirement that the board of auditors must be entirely separate from the board of directors. The overwhelming majority of commenters did not believe a sunset provision for the exemption would be appropriate.¹⁶⁵

Accordingly, we are making several modifications to the exemption as adopted. Under the final rule, the listing of securities of a foreign private issuer will be exempt from all of the audit committee requirements if the issuer meets the following requirements:

- The foreign private issuer has a board of auditors (or similar body), or has statutory auditors (collectively, a "Board of Auditors"), established and selected pursuant to home country legal or listing provisions expressly requiring or permitting such a board or similar body;

- The Board of Auditors is required to be either separate from the board of directors, or composed of one or more members of the board of directors and one or more members that are not also members of the board of directors;

- The Board of Auditors are not elected by management of the issuer and no executive officer of the issuer is a member of the Board of Auditors;

- Home country legal or listing provisions set forth or provide for standards for the independence of the Board of Auditors from the issuer or the management of the issuer;

- The Board of Auditors, in accordance with any applicable home country legal or listing requirements or the issuer's governing documents, is responsible, to the extent permitted by law, for the appointment, retention and oversight of the work of any registered public accounting firm engaged (including, to the extent permitted by law, the resolution of disagreements

between management and the auditor regarding financial reporting) for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for the issuer; and

- The remaining requirements in the rule, such as the complaint procedures requirement, advisors requirement and funding requirement, apply to the Board of Auditors, to the extent permitted by law.

This revised formulation is designed to address the jurisdictions that provide for boards of auditors or similar structures. In all instances, the requirements described in the revised exemption are to apply consistent with home country requirements. We recognize that while these bodies are designed to provide independent oversight of outside auditors, they may not meet all of the same requirements or have all of the responsibilities set forth in Exchange Act rule 10A-3. This approach nonetheless is a preferable method of implementing the protections of the Sarbanes-Oxley Act against the backdrop of this particular category of conflicting home country governance framework.

We have eliminated the requirement that the issuer must also be listed on a market outside the U.S. Also, we are not adopting a sunset date for the exemption. Finally, despite some commenters suggestions, we have not extended the relief to foreign private issuers that have audit committees.¹⁶⁶

vii. Requests for Other Foreign Exemptions

A foreign private issuer availing itself of the exemptions discussed in this section will be subject to specific disclosure requirements discussed in section II.G.1 below. Consistent with our proposal, there will be no other ability for an SRO to exempt or waive foreign issuers from the requirements. In adopting these exemptions, we recognize that some foreign jurisdictions continue to have historical structures that may conflict with maintaining audit committees meeting the requirements of section 10A(m) of the Exchange Act. We encourage foreign issuers that access the U.S. capital markets to continue to move toward internationally accepted best practices in corporate governance.¹⁶⁷ We also understand that corporate

governance structures throughout the world will continue to evolve, and that all future conflicts cannot be anticipated at this time. Accordingly, as requested by many commenters,¹⁶⁸ the Commission has the authority to respond to, and will remain sensitive to, the evolving standards of corporate governance throughout the world to address any new conflicts that may arise with foreign corporate governance rules and practices that cannot be anticipated at this time.

b. Small Businesses

Section 10A(m) of the Exchange Act makes no distinction based on an issuer's size. As discussed in the Proposing Release, we think that improvements in the financial reporting process for companies of all sizes are important for promoting investor confidence in our markets. In this regard, because there have been instances of financial fraud at small companies as well as at large companies, we think that improving the effectiveness of audit committees of small and large companies is important.¹⁶⁹ The final rule, therefore, applies to listed issuers of all sizes as proposed.

The majority of commenters generally agreed with this approach and did not support lesser standards for smaller issuers.¹⁷⁰ These commenters did not believe the requirements will impose a disproportionate burden on small issuers. A few commenters, however, were concerned that smaller issuers may have particular difficulty locating qualified audit committee candidates that will meet the independence criteria, especially given the implementation period proposed by the Commission.¹⁷¹ While these commenters advocated various approaches, such as an exceptional and limited circumstances exemption for smaller issuers or SRO authority to exempt individual small issuers on a case-by-case basis, most agreed that an additional initial implementation period would be appropriate for these issuers.

We recognize that because the final rule applies only to listed issuers, quantitative listing standards applicable to listed securities, such as minimum revenue, market capitalization and

¹⁶³ See, e.g., the Letters of ABA, Cleary; Internet Initiative Japan, Inc.; FSA; Japanese Ministry of Economy, Trade and Industry; Nippon Keidanren; Linklaters; NYSE; S&C.

¹⁶⁴ See, e.g., the Letters of Perusahaan Perseroan (Persero) PT Telekomunikasi Indonesia Tbk; S&C.

¹⁶⁵ Compare, e.g., the letters of ABA; FSA; Japanese Ministry of Economy, Trade and Industry; Nippon Keidanren; Japan Corporate Auditors Association; Matsushita; Nomura Holdings, Inc.; NTT DoCoMo, Inc.; NYSE; ORIX Corporation with the letters of CalPERS; PwC.

¹⁶⁶ See, e.g., the Letters of FSA; Japanese Ministry of Economy, Trade and Industry; Nippon Keidanren; Matsushita; Nomura Holdings, Inc.; PwC; ORIX Corporation; S&C.

¹⁶⁷ See, e.g., IOSCO Principles of Auditor Independence and the Role of Corporate Governance in Monitoring an Auditor's Independence (2002); OECD Principles of Corporate Governance (1999).

¹⁶⁸ See, e.g., the Letters of AFEP-AGREF; Assonime; Cleary; NYSE.

¹⁶⁹ See Beasley, Carcello and Hermanson, *Fraudulent Financial Reporting: 1987-1997, An Analysis of U.S. Public Companies* (Mar. 1999) (study commissioned by the Committee of Sponsoring Organizations of the Treadway Commission).

¹⁷⁰ See, e.g., the Letters of CalPERS; CBA; CSC; Deloitte; PwC.

¹⁷¹ See, e.g., the Letters of ABA; Amex; Nasdaq.