

have audit committees. However, these audit committees may not meet all of the requirements of the final rule. Smaller companies may constitute a larger representative share of issuers that do not meet the requirements, particularly the independence requirements. However, we recognize that because the requirements apply only to listed issuers, the quantitative listing standards applicable to listed securities, such as minimum revenue, market capitalization and shareholder equity requirements, will limit the size of issuers that will be affected by the requirements. Nevertheless, we are providing an additional transition period for smaller issuers to alleviate some of the potential burdens they may face. We are also providing an additional transition period for foreign issuers. Companies that do not currently meet the requirements will face all of the costs described above. However, these entities, because they currently lack the protections provided by the standards, may bear a disproportionately greater risk of fraudulent financial reporting, and thus may reap proportionately greater benefits.

We also are adopting limited exemptions to the requirements, such as an exemption for multiple listings, a limited exemption for new public companies and exemptions for certain foreign issuers, to alleviate some of the burdens companies may face where consistent with investor protection. Commenters expressed overwhelming support for these exemptions which will alleviate unnecessary costs and burdens companies may face without any attendant loss in investor protection. Companies that perceive the requirements as too onerous could be dissuaded from seeking or maintaining a listing for their securities, which could impact capital formation and negatively impact the transparency and liquidity of its securities.

We requested comment on the type, amount and duration of these costs. We received no specific data in response to our request. We have no reliable basis for estimating the actual number of companies that will face increased costs as a result of Exchange Act Section 10A(m) or the amount of such costs.

With respect to the disclosure changes regarding audit committees, issuers subject to the proxy rules are already required to compile most of this information for proxy or information

statements where directors are being elected. Foreign private issuers that file their annual reports on Form 20-F also are already required to identify the members of their audit committee. The disclosure regarding if a listed issuer is availing itself of an exemption to the requirements should result in minimal additional disclosure. Using estimates derived from our Paperwork Reduction Act analysis, we estimated that the incremental impact of our disclosure changes will result in a total cost of \$112,525 for all affected companies.²⁵³

In formulating the final amendments, we considered several regulatory alternatives that would be consistent with the specific mandate required by section 10A(m) of the Exchange Act. For example, we considered the propriety of excluding all foreign issuers, issuers of a particular size or additional classes of securities, but we determined that such an exclusion would not be appropriate or consistent with the policies underlying the Sarbanes-Oxley Act. The overwhelming majority of commenters agreed with this approach. We think that improvements in the financial reporting process for all listed issuers are important for promoting investor confidence in our markets.

We also considered whether we should provide objective guidance for determining who is an "affiliated person" for purposes of the independence requirement. While the majority of commenters supported a safe harbor, some did not want a safe harbor for fear any thresholds in the safe harbor would be viewed as a ceiling that would disqualify a director from serving on the audit committee. In considering the uncertainty that may arise in determining whether a person is an "affiliated person," we have adopted a safe harbor from the definition of affiliate for non-investment companies. However, to add clarity we have added explicit language specifying that the thresholds in the safe harbor are not designed to be viewed as an upper limit on permissible levels.

We have also adopted other limited exemptions to alleviate some of the burdens companies may face where consistent with the Sarbanes-Oxley Act

and investor protection. We have expanded these exemptions in a number of instances, where consistent with the Sarbanes-Oxley Act and investor protection, to alleviate unnecessary burdens and expenses. We believe the final rule reflects an appropriate balance between investors and investor groups who advocated more stringent requirements and issuers and their representatives who requested a much larger expansion of the exemptions.

V. Consideration of Burden on Competition and Promotion of Efficiency, Competition and Capital Formation

Section 23(a)(2) of the Exchange Act²⁵⁴ requires us, when adopting rules under the Exchange Act, to consider the impact that any new rule would have on competition. In addition, section 23(a)(2) prohibits us from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

The amendments represent the implementation of a Congressional mandate. They are intended to increase the independence and effectiveness of listed company audit committees. We anticipate these requirements will enhance the proper functioning of the capital markets by increasing the quality and accountability of financial reporting and restoring investor confidence. This increases the competitiveness of companies participating in the U.S. capital markets. However, the requirements relate only to companies listed on a national securities exchange or national securities association. Competitors not subject to the standards specified in section 10A(m) of the Exchange Act may be subject to fewer corporate governance burdens. Similarly, to the extent foreign exchanges or other markets do not impose these standards, competitors could, all things being equal, migrate to those markets to avoid compliance. This could cause U.S. exchanges and securities associations to lose trading volume and investors to lose liquidity or the benefits of trading in a U.S. market. Competitors and markets not subject to the standard, however, also may suffer from decreased investor confidence compared to those that do comply with the new standards.

Section 2(b) of the Securities Act,²⁵⁵ section 3(f) of the Exchange Act²⁵⁶ and section 2(c) of the Investment Company

90; AICPA, Codification of Statements on Auditing Standards ("AU") § 380; Independence Standards Board, "Independence Discussion with Audit Committees," Independence Standard No. 1 (Jan. 1999).

²⁵³ The estimate is based on the burden hour estimates calculated under the Paperwork Reduction Act. For purposes of the Paperwork Reduction Act, we estimate that the additional disclosure will result in 401 internal burden hours and \$62,400 in external costs. Assuming a cost of \$125/hour for in-house professional staff, the total cost for the internal burden hours would be \$50,125. Hence the aggregate cost estimate is \$112,525 (\$50,125 + 62,400). The \$125/hour cost estimate is based on data obtained from *The SIA Report on Management and Professional Earnings in the Securities Industry* (Oct. 2001).

²⁵⁴ 15 U.S.C. 78w(a)(2).

²⁵⁵ 17 U.S.C. 77b(b).

²⁵⁶ 15 U.S.C. 78c(f).