

In formulating our proposals, we considered several regulatory alternatives that would be consistent with the specific mandate required by Section 10A(m) of the Exchange Act. We considered the propriety of excluding all foreign issuers or issuers of a particular size, but such an exclusion may not be appropriate or consistent with the policies underlying the Sarbanes-Oxley Act. 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 proposed independence requirement. In considering the uncertainty that may arise in determining whether a person is an "affiliated person," we have proposed a safe harbor from the definition of affiliate for non-investment companies. We have also proposed other limited exemptions to alleviate some of the burdens companies may face where consistent with investor protection.

#### *D. Request for Comments*

We request that commenters provide views and supporting information as to the benefits and costs associated with the proposals. We seek estimates of these costs and benefits, as well as any costs and benefits not already identified. We also request comment regarding the relative costs and benefits of pursuing alternative regulatory approaches that are consistent with the Sarbanes-Oxley Act's statutory mandate.

### **V. Consideration of Impact on the Economy, Burden on Competition and Promotion of Efficiency, Competition and Capital Formation**

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA,"<sup>146</sup> we solicit data to determine whether the proposals constitute a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results or is likely to result in:

- An annual effect on the economy of \$100 million or more (either in the form of an increase or a decrease);
- A major increase in costs or prices for consumers or individual industries; or

<sup>145</sup>\$85,625. Hence the aggregate cost estimate is \$185,225 (\$99,600 + \$85,625). 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).

<sup>146</sup>Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

- Significant adverse effects on competition, investment or innovation. We request comment on the potential impact of the proposals on the economy on an annual basis. Commenters are requested to provide empirical data and other factual support for their views if possible.

Section 23(a)(2) of the Exchange Act<sup>147</sup> 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 proposals represent the implementation of a Congressional mandate. They are intended to increase the independence and effectiveness of listed company audit committees. We anticipate these proposals would 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, our specific proposals 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 less 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. 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.

We request comment on whether the proposed amendments, if adopted, would impose a burden on competition. Commenters are requested to provide empirical data and other factual support for their views if possible.

Section 2(b) of the Securities Act,<sup>148</sup> Section 3(f) of the Exchange Act<sup>149</sup> and Section 2(c) of the Investment Company Act<sup>150</sup> require us, when engaging in rulemaking where we are required to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the

protection of investors, whether the action will promote efficiency, competition, and capital formation. The proposals would enhance the quality and accountability of the financial reporting process and may help increase investor confidence, which implies increased efficiency and competitiveness of the U.S. capital markets. Increased market efficiency and investor confidence also may encourage more efficient capital formation. As noted above, however, the proposals could have certain indirect negative effects, such as inconsistent application across all competitors. In addition, the proposed standards, while providing great flexibility for implementation, do remove a certain amount of individual control over the corporate governance process, which could have the possible effect of stifling more efficient approaches from being implemented if they were to develop.

If a company found the proposed requirements too onerous, it could be dissuaded from accessing the public capital markets, which could impact capital formation. The possibility of these effects and their magnitude if they were to occur are difficult to quantify. We have proposed several limited exemptions from the requirements to alleviate some of the burdens companies may face where consistent with investor protection. For example, the proposed limited exemption for new public companies is intended to counteract any disincentive the proposed requirements may have on a company's willingness to access the public capital markets.

We request comment on whether the proposed amendments, if adopted, would promote efficiency, competition, and capital formation. Commenters are requested to provide empirical data and other factual support for their views if possible.

### **VI. Initial Regulatory Flexibility Analysis**

This Initial Regulatory Flexibility Analysis, or IRFA, has been prepared in accordance with the Regulatory Flexibility Act.<sup>151</sup> This IRFA involves proposals to direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with several enumerated standards relating to the issuer's audit committee.

#### *A. Reasons for, and Objectives of, Proposed Amendments*

We are proposing new Exchange Act Rule 10A-3 to comply with the mandate

<sup>147</sup>15 U.S.C. 78w(a)(2).

<sup>148</sup>17 U.S.C. 77b(b).

<sup>149</sup>15 U.S.C. 78c(f).

<sup>150</sup>15 U.S.C. 80a-2(c).

<sup>151</sup>5 U.S.C. 603.