

exposing such persons to increased liability. In response to these comments, we have created a safe harbor from liability for audit committee financial experts. This safe harbor states that an audit committee financial expert is not deemed an expert for any purpose, including for purposes of Section 11 of the Securities Act, which imposes, in private actions, a liability standard that is more strict than typically imposed by the anti-fraud provisions of the Securities Act and the Exchange Act. In addition, the safe harbor states that a person's potential liability as a director does not change as a result of being designated an audit committee financial expert. That person will be subject to the same duties, obligations and liability to which he or she would have been subject, absent such designation. The safe harbor also clarifies that the designation of an audit committee financial expert does not affect the duties, obligations and liability of other directors and audit committee members.

VI. Final Regulatory Flexibility Analysis

This Final Regulatory Flexibility Analysis has been prepared in accordance with 5 U.S.C. 603. It relates to revisions to Exchange Act Form 8-K, Form 10-K, Form 10-KSB, Form 20-F, Form 40-F, Regulation S-K and Regulation S-B.

A. Need for, and Objectives of, the Amendments

We are adopting these disclosure requirements to comply with the mandate of, and fulfill the purposes underlying the provisions of, the Sarbanes-Oxley Act of 2002. The new disclosure items are intended to enhance investor confidence in the fairness and integrity of the securities markets by increasing transparency as to whether a company has an audit committee financial expert on its audit committee and whether a company has adopted a code of ethics that applies to its principal executive officer and senior financial officers. We believe that these rules will help investors to understand and assess certain aspects of a company's corporate governance.

B. Significant Issues Raised by Public Comment

The Initial Regulatory Flexibility Analysis, or IRFA, appeared in the Proposing Release. We requested comment on any aspect of the IRFA, including the number of small entities that would be affected by the proposals, the nature of the impact, how to quantify the number of small entities

that would be affected and how to quantify the impact of the proposals.

A number of commenters expressed concern that small business issuers, including small entities, would be particularly disadvantaged by the proposed definition of "audit committee financial expert," which they thought was too restrictive. Commenters believed that such entities may be more likely to be unable to attract qualified persons to serve on their audit committees and that a higher percentage of small companies than large companies would be compelled to state that they had no audit committee financial expert. They suggested that this problem would be exacerbated for companies whose operations are primarily conducted in relatively small geographic regions in which such expertise may not be available.

C. Small Entities Subject to the New Disclosure Requirements

The new disclosure items affect issuers that are small entities. Exchange Act Rule 0-10(a)⁷⁵ defines an issuer, other than an investment company, to be a "small business" or "small organization" if it had total assets of \$5 million or less on the last day of its most recent fiscal year. We estimate that there are approximately 2,500 issuers, other than investment companies, that may be considered small entities. The new disclosure items apply to any small entity that is subject to Exchange Act reporting requirements.

D. Projected Reporting, Recordkeeping, and Other Compliance Requirements

The new disclosure items require companies to disclose information as to whether an audit committee financial expert serves on the company's audit committee and whether the company has adopted a code of ethics that applies to its principal executive officer and senior financial officers. All small entities that are subject to the reporting requirements of Section 13(a) or 15(d) of the Exchange Act are subject to these disclosure requirements. Because reporting companies already file the forms being amended, no additional professional skills beyond those currently possessed by these filers are necessary to prepare the new disclosure. We expect that these new disclosure items will increase costs incurred by small entities by requiring them to compile and report new information. In addition, to the extent that some small entities may have difficulty attracting qualified audit committee financial experts, disclosure that they have no

audit committee financial expert may have a negative impact on the market price of their securities. We have calculated for purposes of the Paperwork Reduction Act that each company, including a small entity, would be subject to an added annual reporting burden of approximately 2.1 hours and an estimated annual average cost of approximately \$206 for disclosure assistance from outside counsel as a result of the amendments. These burden estimates reflect only the burden and cost of the required collection of information. They do not reflect any potential burden or cost associated with recruitment of a qualified audit committee financial expert or creation of a code of ethics, neither of which is required by our rules.

E. Agency Action To Minimize Effect on Small Entities and Significant Alternatives

The Regulatory Flexibility Act directs the Commission to consider significant alternatives that would accomplish the stated objective, while minimizing any significant adverse impact on small entities. In connection with the new disclosure items, we considered the following alternatives: (a) The establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (b) the clarification, consolidation, or simplification of the reporting requirements for small entities; (c) the use of performance rather than design standards; and (d) an exemption from coverage of the requirements, or any part thereof, for small entities.

We believe that different compliance or reporting requirements for small entities would interfere with the primary goal of increasing transparency of corporate governance. Although we generally believe that an exemption for small entities from coverage of the new disclosure requirements is not appropriate and would be inconsistent with the policies underlying the Sarbanes-Oxley Act, we have provided a deferred compliance date for small business issuers, including those that constitute small entities, with respect to the required audit committee financial expert disclosures.⁷⁶ Under the adopted

⁷⁵ Item 10 of Regulation S-B (17 CFR 228.10) defines a small business issuer as a company that has revenues of less than \$25 million, is a U.S. or Canadian issuer, is not an investment company, and has a public float of less than \$25 million. Also, if it is a majority owned subsidiary, the parent corporation also must be a small business issuer. Rule 0-10 of the Exchange Act (17 CFR 240.10) defines a small entity for purposes of the Regulatory

⁷⁶ 17 CFR 240.0-10(a).