PKF PERSPECTIVES

UPDATE FOR PUBLIC AND PRIVATE COMPANIES

PUBLIC COMPANY DEVELOPMENTS

Non-Accelerated Filers Exempted from SOX 404(b)

Under the provisions of Section 404 of the ***Sarbanes-Oxley Act of 2002*** (SOX 404), publicly reporting companies, under SOX 404(a), and their independent auditors, under 404(b), are each required to report on the effectiveness of internal control over financial reporting.

Non-accelerated filers (public companies with a public float below $75 million) were previously temporarily exempted from the SOX 404(b) audit requirement, but would have had to comply for fiscal years ending on or after June 15, 2010. At the time of that deferral, the Securities and Exchange Commission (SEC) was adamant that it would not be granting any further extensions for compliance with SOX 404(b).

On July 21, 2010 President Obama signed into law the ***Dodd-Frank Wall Street Reform and Consumer Protection Act***. The Dodd-Frank Act permanently exempts non-accelerated filers and debt-only issuers from the requirements of Section 404(b). In brief, it states:

1. SOX 404(b) shall not apply with respect to any audit report prepared for an issuer that is neither a *large accelerated filer* nor an *accelerated filer* as defined.

2. The SEC shall conduct a study to determine how it could reduce the burden of complying with SOX 404(b) for companies whose market capitalization is between $75 million and $250 million while maintaining investor protections for such companies.

3. The study shall also consider whether reducing the compliance burden or completely exempting such companies from compliance with SOX 404(b) would encourage companies to list on exchanges in the United States in their initial public offerings. The SEC needs to submit their report to Congress within nine months.

The consequence of this exemption is that non-accelerated filers will not be required to provide auditor attestation reports on internal control over financial reporting in their annual reports, and significantly reduces the anticipated compliance burdens of smaller reporting companies. Disclosure of management attestations on internal control over financial reporting continues to be required.

It is expected that these revisions will apply retroactively to non-accelerated filers with fiscal years that ended before July 21, 2010 (e.g., non-accelerated filers with a June 30, 2010 fiscal year-end).

SEC Updates Financial Reporting Manual as of March 31, 2010

On July 7, 2010 the staff of the SEC Division of Corporation Finance posted an updated version of the online Financial Reporting Manual (Manual) as of March 31, 2010. The Manual is a comprehensive source of SEC staff interpretations on financial reporting matters (even though it is designed only to be an internal reference document to provide guidance to the SEC's Division of Corporation Finance staff).

GAAP FOR PRIVATE COMPANIES

A Step Closer

In February this year, we reported on the intensifying debate over the need for separate accounting rules for privately-held companies, and the formation of a Blue-Ribbon Panel on Private Company Financial Reporting (the Panel) in December 2009, sponsored by the American Institute of Certified Public Accountants (AICPA), the Financial Accounting Foundation (the FAF), which is the parent organization of the Financial Accounting Standards Board (FASB), and the National Association of State Boards of Accountancy (NASBA). The purpose of the 18-member Panel is to provide recommendations on the future of U.S. accounting standards for private companies by the end of this year, including considering the process of standard-setting and recommending whether private companies need their own version of U.S. generally accepted accounting principles (U.S. GAAP).

At their meeting on July 19, 2010, the Panel weighed in on seven alternative models based on U.S. GAAP and International Financial Reporting Standards (IFRS), and — in what is perhaps a surprising move — eliminated from further consideration models that are based on IFRS. IFRS already has its own separate set of guidelines for private companies, called IFRS for small and medium-sized entities (SMEs), which offers private companies a significantly slimmed-down version of IFRS. Less surprisingly, the group also eliminated a model that effectively would have maintained the status quo.

All of the remaining models under consideration would result in differences in U.S. GAAP for privately-held companies, where warranted, compared with U.S. GAAP for public companies.

The Panel has decided to further consider three of the U.S. GAAP-based models and develop two or three hybrid models that are more detailed and focused.

The three models that are advancing for further consideration are:

- ***U.S. GAAP with exclusions for private companies with enhancements.***
- ***U.S. GAAP as a baseline with public company add-ons.***
- ***Separate, stand-alone U.S. GAAP based on current U.S. GAAP.***

The Panel recommended exposing a series of questions related to the potential standard-setting models for public comment through the FASB's website by the end of July to ensure that it isn't leaving out any critical elements or pieces of information for consideration.

All comments will be made public on the FASB website and the Panel's staff plans to summarize the comments and present them to the Panel members at their next meeting on October 8, 2010. The Panel aims to have any recommendations ironed out by its December 10, 2010 meeting.

The Panel agreed that selecting a model that is relevant to the users of private company financial reports should be the No. 1 focus moving forward. The aim is to make the financial statements more useful and better for the intended audience of those statements.

Regardless of which model the Panel eventually selects to recommend, several members said the group that sets those standards needs to understand the needs of the users for whom they are designing the standards. Discussion at the meeting therefore included what body should set accounting standards for private companies.

Most of the Panel members expressed concern with the current makeup of the FASB and noted its heavy, albeit appropriate, focus on public companies. As such, discussions centered around whether the FASB should make efforts to set private company accounting standards, whether a restructured FASB with greater private company representation is needed, and/or whether a new separate private company accounting reporting standards-setter, under the oversight of FAF, is needed.

AICPA President and CEO Barry Melancon advocated a board separate from FASB to oversee private company accounting standards:

> *I believe it isn't practical to have one board set both private and public company standards. ... I believe FAF should establish a separate board for private companies, let the currently constructed FASB still drive the train and set public company standards, but have the new board constituted solely with individuals that are focused on private companies decide whether, what and how U.S. GAAP should apply to private companies starting with the FASB standards.*

We will keep you posted.

PKF

29 Broadway ✦ New York, NY 10006
Telephone: (212) 867-8000 ✦ Telefax: (212) 687-4346
www.pkfnewyork.com ✦ E-mail: info@pkfny.com

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