

Advocacy Supports the Securities and Exchange Commission's Forthcoming Sarbanes-Oxley Management Guidance

On September 15, 2006, the Office of Advocacy (Advocacy) sent a letter to the U.S. Securities and Exchange Commission (SEC) in response to the notice, *Concept Release Concerning Management's Reports on Internal Control Over Financial Reporting*. Advocacy commends the SEC for starting to develop management guidance that will help small public companies comply with Section 404 of the Sarbanes-Oxley Act of 2002. On September 14, 2006, Advocacy submitted comments on the proposed rule extending the compliance deadlines to Section 404 for smaller and newly public companies. Advocacy encouraged the SEC to explore more opportunities for reducing Sarbanes-Oxley costs on small businesses. A copy of Advocacy's letter to the SEC may be accessed at <http://www.sba.gov/advo/laws/comments/>.

- The Securities and Exchange Act of 1934 requires audited quarterly and annual financial reports from some public companies to be filed with the SEC. Companies have systems in place at various levels of decision-making to guard against fraudulent or mistaken transactions and to ensure the accuracy of the financial reports submitted to the SEC. These systems are generally referred to as "internal controls."
- The Sarbanes-Oxley Act of 2002 introduced a new requirement for companies that submit audited financial reports to the SEC to include with their annual report internal control reports. Section 404(a) requires that management assess the effectiveness of its company's financial reports, by identifying any risks to financial reporting and designing appropriate internal controls that address those risks. Section 404(b) requires an external auditor to report on whether the management's assessment is fairly stated and effective.
- In the absence of management guidance, public companies have followed the Auditing Standard No.2 (AS2) of the Public Companies Accounting Oversight Board (PCAOB), a guide created for external auditors and accountants to assess standard public companies. Many small companies utilizing the broad AS2 framework found it caused excessive and unnecessary testing of internal controls. Advocacy supports a revision to AS2, and commented that the management guidance should be easily accessible and understandable to members of the small business community.

For more information, visit Advocacy's Web page at <http://www.sba.gov/advo>, or contact Assistant Chief Counsel Janis Reyes by email at Janis.Reyes@sba.gov or by phone at 202-619-0312.