

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 52006 / July 11, 2005**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 2274 / July 11, 2005**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-11977**

**In the Matter of**  
  
**Foamex International, Inc.,**  
  
**Respondent.**

**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”), against Foamex International, Inc. (“Foamex”).

**II.**

In anticipation of the institution of these proceedings, Foamex has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Foamex consents to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist Order Pursuant to Section 21C of the Securities Exchange Act of 1934 (“Order”), as set forth below.

### III.

On the basis of this Order and Foamex's Offer, the Commission finds that:

#### **Respondent**

1. Foamex, a Delaware corporation based in Linwood, Pennsylvania, manufactures and distributes flexible polyurethane and advanced polymer foam products. Foamex's common stock is registered under Section 12(g) of the Exchange Act and is traded on the NASDAQ National Market System.

#### **Summary**

2. This matter involves Foamex's need to address deficiencies in its internal accounting controls. Since at least 1999, Foamex's auditors have advised the company that these internal control deficiencies created "reportable conditions."<sup>1</sup> In particular, the auditors identified internal control deficiencies in Foamex's: (i) information technology systems; (ii) inventory procedures, processes and systems; and (iii) preparation of quarterly financial reports. In addition, since 1999, Foamex restated many of its interim financial reports because of material errors in its financial statements which resulted, in part, from its internal control issues. For example, in January 2004, Foamex had to restate its financial reports for the first three quarters of 2003 due to an overstatement of certain inventory. Foamex, under new management, has engaged in meaningful efforts to remediate the reportable conditions. However, the repeated findings of its auditors with respect to certain reportable conditions show that Foamex did not undertake such remediation on a timely basis.

#### **Discussion**

3. Through a series of acquisitions between 1983 and 2001, Foamex's operations expanded to encompass over fifty manufacturing and distribution facilities in the United States, Canada and Mexico. The companies Foamex acquired utilized different accounting procedures, computer systems and software, and Foamex did not integrate all of these systems. These differing systems, particularly those related to inventory, created inconsistencies in the company's books and records, which the company did not reconcile in a timely manner.

4. In August 1999, Foamex's auditor notified Foamex's Audit Committee that Foamex needed to improve its internal controls. In particular, the auditor reported that Foamex's systems for the preparation of interim financial information did not provide an adequate basis for the auditor to complete, prior to certain filing deadlines, its reviews of Foamex's interim financial statements.

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<sup>1</sup> A *reportable condition* is a significant deficiency in the design or operation of an internal control, which could adversely affect the organization's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. AICPA Statement on Auditing Standards No. 60.

5. In May 2000, Foamex's auditor issued a Report to Management in connection with its audit of Foamex's financial statements for the year ended December 31, 1999. In that report, Foamex's auditor identified reportable conditions and recommended that Foamex: (i) make significant improvements in the control environment and reporting practices of Foamex's foreign operations; (ii) conduct a comprehensive analysis of financial results on a quarterly basis; (iii) improve inventory reporting; and (iv) develop a comprehensive information technology ("IT") strategy, including an enterprise-wide security program.

6. In February and March 2001, in connection with its audit of Foamex's financial statements for the year ended December 31, 2000, Foamex's auditor advised Foamex's Audit Committee of reportable conditions similar to those above. In June 2001, Foamex's auditor resigned and, in July 2001, Foamex retained a new auditor.

7. Although Foamex's prior management informed the Commission's staff in mid-2002 that the company was initiating prompt corrective actions to address its internal control deficiencies, its new auditor issued a report to Foamex's Audit Committee in March 2003. The report identified reportable conditions similar to those previously identified by Foamex's prior auditor: (i) oversight of financial reporting by international subsidiaries; (ii) inventory procedures, processes and systems; (iii) integration of IT systems; (iv) access and security for IT systems; and (v) process for reviewing and approving journal entries.

8. In January 2004, Foamex restated its financial reports for the first three quarters of 2003 because it had overstated its in-transit raw material inventory. This error, which has been corrected, occurred during Foamex's implementation of a new system to calculate the value of certain in-transit raw material inventory. In particular, the new system failed to apply certain rebates, resulting in inaccurate inventory values.

9. In March 2004, Foamex's auditor issued a report to Foamex's Audit Committee identifying four reportable conditions, three of which had been previously identified. The reportable conditions pertained to: (i) the integration of IT systems; (ii) access and security for IT systems; (iii) inventory procedures, processes and systems; and (iv) quarterly financial reporting.

10. In April 2004, Foamex's Audit Committee retained a new auditor. Foamex, under the mandate of a new management team, has initiated steps to remediate the reportable conditions. It has strengthened financial management through the hiring of additional financial and accounting personnel and continues to implement an enterprise-wide IT system. Foamex has also retained, through its counsel, a special consultant on internal accounting controls. Nevertheless, the repeated observations of the auditors and Foamex's history of restating its interim financial reports show that Foamex did not devote the appropriate managerial effort and other resources to remediate its deficient internal controls, which were identified as reportable conditions in 1999. As a result, Foamex encountered undue delays in implementing an effective remediation program.

## Violations

11. As a result of the conduct described above, Foamex violated:
  - a. Section 13(a) of the Exchange Act, which requires reporting companies to file periodic and other reports with the Commission containing such information as the Commission's rules prescribe, and Rule 13a-13, promulgated pursuant to Section 13(a) of the Exchange Act, which requires issuers to file accurate quarterly reports with the Commission on a Form 10-Q.
  - b. Section 13(b)(2)(A) of the Exchange Act, which requires all reporting companies to make and keep books, records, and accounts, which, in reasonable detail, accurately reflect the transactions and dispositions of assets; and
  - c. Section 13(b)(2)(B) of the Exchange Act, which requires all reporting companies to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles and to maintain accountability of assets.

## Undertakings

12. Foamex undertakes to:
  - a. Cooperate fully with its auditors in connection with their audit of Foamex's financial statements, which will include, in accordance with Section 404 of the Sarbanes-Oxley Act of 2002, 15 U.S.C. § 7262, a review and evaluation of Foamex management's assessment of internal control over financial reporting as well as a report containing an opinion on the effectiveness of Foamex's internal control over financial reporting. Foamex shall, on a timely basis, provide the auditors with access to its files, books, records and personnel as reasonably requested for the review. In connection therewith, the auditors will issue a written report ("Section 404 Report") to Foamex's Audit Committee with regard to whether it concurs with management's assessment of internal control over financial reporting and will address any significant deficiencies, as defined in Auditing Standard No. 2 of the Public Company Accounting Oversight Board,<sup>2</sup>

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<sup>2</sup> A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the company's ability to initiate, authorize, record, process, or report external financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the company's annual or interim financial statements that is more than inconsequential will not be prevented or detected. Public Company Accounting Oversight Board Bylaws and Rules – Standards – AS2 (Mar. 9, 2004).

that it has identified and that were not identified and remediated by management. Promptly after receipt of the Section 404 Report, Foamex's Audit Committee will forward the Section 404 Report to the Commission's staff and to Foamex's Special Consultant, which was previously retained through its counsel.

b. Require the Special Consultant to review the Section 404 Report and issue a written report ("Special Consultant Report") to Foamex's Audit Committee and the Commission's staff. The Special Consultant Report shall include recommendations relating to modifications of, or additions to, internal control over financial reporting to address the significant deficiencies identified in the Section 404 Report, as well as procedures to implement such modifications or additions. The Special Consultant Report shall be issued no later than 90 days following the issuance of the Section 404 Report or such other date mutually agreed upon by Foamex and the Commission's staff after consultation with the Special Consultant.

c. Adopt all recommendations in the Special Consultant Report, provided, however, that within 30 days after the Special Consultant delivers the Special Consultant Report, Foamex shall in writing advise the Special Consultant and the Commission's staff of any recommendations that it considers unduly burdensome, impractical or costly. Foamex need not adopt such recommendations at that time but shall propose in writing an alternative policy, procedure, or system designed to achieve the same objective or purpose. As to any recommendation on which Foamex and the Special Consultant do not agree, such parties shall attempt in good faith to reach an agreement within 30 days after Foamex delivers the written advice. In the event Foamex and the Special Consultant are unable to agree on an alternative proposal, Foamex shall abide by the determinations of the Special Consultant.

d. Require the Special Consultant to review Foamex's progress in correcting significant deficiencies, if any, identified in the Section 404 Report and to provide a written report to the Audit Committee and the Commission's staff on the status of Foamex's remediation efforts each calendar quarter thereafter until the reported deficiencies have been remediated, provided that such remediation efforts shall be completed no later than 18 months from the date that Foamex receives the Special Consultant Report.

e. For good cause shown, and upon receipt of a timely application from the Special Consultant or Foamex, the Commission's staff may extend any of the procedural dates set forth above.

### **Foamex's Remedial Efforts**

13. In determining to accept the Offer, the Commission considered remedial acts undertaken by Foamex's new management and cooperation afforded the Commission's staff.

#### **IV.**

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Foamex's Offer.

Accordingly, it is hereby ORDERED that:

A. Foamex cease and desist from committing or causing any violations and any future violations of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rule 13a-13 thereunder.

B. Foamex shall comply with the undertakings enumerated in Section III.12. above.

By the Commission.

Jonathan G. Katz  
Secretary