

New Federal Initiatives Project

**The "Startup Expansion and Investment
Act," HR 2941**

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The much-debated Section 404 of the Sarbanes-Oxley Act of 2002 imposed significant cash expenses and compliance burdens on U.S. public companies, through its requirement for expensive certifications of internal control systems by outside auditors. The auditors became extremely risk averse in the this process--which should not have surprised anyone. The expenses then turned out to be much greater than forecast by the SEC or expected by Congress. The burden is disproportionately heavy on smaller companies. This problem was recognized by the Dodd-Frank Act of 2010, of which Section 989G permanently exempted companies with a market capitalization held by non-affiliates of less than \$75 million from the requirements of Section 404(b) – making one deregulatory correction in the midst of a vast expansion of regulation.

Congressman Ben Quayle and several co-sponsors introduced a bill on September 15, 2011, the "Startup Expansion and Investment Act," HR 2941, with the goal of further reducing the regulatory burden of Sarbanes-Oxley, and making conversion to a U.S. public company more attractive. This short bill would make *optional* the adoption of Section 404 (a)(2) and (b) for companies with a market capitalization of less than \$1 billion, which have been public for less than ten years. Thus, such companies could decide to adopt these Sarbanes-Oxley procedures and external accountant's attestation, or to opt out of them. A decision to opt out would be required to be reported to investors in the next SEC filings.

The bill "removes one of the many regulatory hurdles that inhibit many companies from going public. Access to the public markets is vital for a company to expand and hire new workers," Congressman Quayle stated.

Such a voluntary regime for Section 404 would create the ability to test whether investors in such companies value the Sarbanes-Oxley provisions or not, by seeing how the securities prices of those companies opting in or out respond.¹

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¹ I have previously proposed that these provisions should be optional for all companies, with stockholder approval. See "Has Sarbanes-Oxley Harmed Entrepreneurs?" May 24, 2007, available at www.aei.org/pollock.

Related Links:

Sarbanes-Oxley Act of 2002
<http://www.sec.gov/about/laws/soa2002.pdf>

Startup Expansion and Investment Act, HR 2941
<http://thomas.loc.gov/cgi-bin/query/z?c112:H.R.2941.IH/>

Pollock, Alex, “Has Sarbanes-Oxley Harmed Entrepreneurs?” *Hudson Institute*
<http://www.aei.org/speech/26375>