

SEC Chief Cox Seen Enforcing Rules; Sympathetic Ear for Small Companies

NO 'INVISIBLE' HAND

By Pat Maio

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Christopher Cox's tenure as head of the Securities and Exchange Commission is only two months old, but early indicators are that he will have a lighter regulatory hand than predecessor William Donaldson, who led the SEC for two years in the wake of accounting scandals at Enron Corp.

The clearest signal of his modulated position involves delaying by a year the implementation of Section 404 of the Sarbanes-Oxley Act, as it applies to public companies with market values of less than \$75 million. The section calls for all public companies to extensively document their internal accounting controls, a process that has proven costly for many businesses.

"When it comes to smaller companies in particular, the commission is keenly sensitive to the differences in controls and procedures that are necessary for the protection of investors," said Cox in a written response to questions from the Orange County Business Journal.

"Armed with the experience of the last three years' implementation of Sarbanes-Oxley, the SEC and the Public Company Accounting Oversight Board are working to encourage both companies and auditors to reduce unnecessary costs and other burdens, so that the benefits of the new requirements can be achieved on a sustainable basis," he said. Donaldson raised the ire of publicly traded companies that thought his approach favored investors at the expense of companies.

"It's a big deal for us," said Marry Lynch, chief financial officer of Irvine-based Diedrich Coffee Inc., which has a market value of \$44 million. "It's a tremendous cost for a company our size to get ready. It doubles our audit costs."

Also, Cox has opposed a rule that requires companies to count stock options as

expenses. As a legislator, Cox proposed laws that would have limited stock options expensing to the top five officers of a company.

The rule, which is being pushed by investor groups, stands to reduce earnings per share and possibly stockprice, particularly for technology companies that typically use options to lure workers.

The law is in effect for companies whose annual reporting period began after July 15. For those whose annual period ends Dec. 31, compliance is required by Jan. 1.

"In a sense, (Cox's proposal) diluted the standard that required expensing of stock options for all of management," said Vivek Mande, director of the center for corporate reporting and governance at California State University, Fullerton.

Cox, who formerly represented the congressional district that covers Newport Beach and Irvine, had said during his confirmation hearing that he wouldn't fight the rule. And in statements over the past few months, the chairman appeared to tow the SEC line, backing the controversial new regulation.

"It doesn't surprise me because he's no longer a politician and lawmaker," said Mande, a former academic fellow with the SEC's office of economic analyses. "He's chairman of the SEC and he's going to pursue the SEC's agenda vigorously."

Another hot button issue is hedge fund oversight. Cox has signaled that he will stand behind an SEC rule requiring hedge fund managers to register by Feb. 1 as "investment advisers" with the SEC. Hedge funds, pools of capital catering mostly to wealthy investors, have come under closer scrutiny from federal regulators in recent years.

"I don't expect any major technical difficulties for newly registering hedge fund advisers," Cox wrote in the e-mail. "Indeed, many hedge fund advisers already are registered with the SEC. This hasn't hampered their growth, or impeded their ability to engage in legitimate investment techniques."

The \$1 trillion hedge fund industry has attracted plenty of attention of late. The SEC went after Bayou Management LLC, a Connecticut-based firm that collapsed after top officers allegedly took more than \$450 million from investors. In late September, the officers pleaded guilty.

Donaldson had pushed through adoption of the hedge fund rule despite strong criticism from Federal Reserve Chairman Alan Greenspan and two Republican-appointed SEC commissioners who said that registration would do little to prevent fraud.

"The new legislation is not a positive or helpful thing," said Charles Martin, who just launched Newport Beach hedge fund Mont Pelerin Capital LLC, with plans to raise more than \$200 million to invest. "The hedge fund industry is basically between sophisticated investors and top investment professionals. Like all industries, there are a few bad apples, but registration will not prevent abuses."