**Companies Complain About Cost Of Corporate-Governance Rules**

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Some U.S. companies are complaining that new rules aimed at improving corporate accountability will cost them in dollars and in time this year. Most of the rules stem from the 2002 Sarbanes-Oxley Act, which Congress enacted to beef up corporate governance in the aftermath of accounting fraud uncovered at Enron Corp., WorldCom Inc. and elsewhere. Written by the Securities and Exchange Commission, the regulations are aimed at toughening corporate accountability to restore investor confidence and are just now starting to hit bottom lines. Advocates say they will help companies avoid costly problems down the road.

"We can't lose sight of the fact that we came close to an all-out breakdown of investor trust in financial statements and the integrity of the financial-reporting process," says Charles Mulford, an accounting professor at the Georgia Institute of Technology.

While there is agreement that governance rules are needed, some companies cited the increased cost of complying. "The real cost isn't the incremental dollars, it is having people that should be focused on the business focused instead on complying with the details of the rules," said Peter Bible, chief accounting officer at General Motors Corp. "Everybody feels they have to do something to react to the corporate scandals, [but] you really have to scratch your head and say, 'How is this really benefiting our shareholders?' "

The rules are coming into effect at a time when corporations already are battling other increasing costs, including health-care expenses. Even before the most expensive Sarbanes-Oxley rules take effect, companies say their audit costs are increasing by as much as 30% or more this year due to tougher audit and accounting standards, including complex rules to bring more off-balance-sheet items onto the books. Companies also are paying steep fees to fund a new accounting-oversight board -- as much as $2 million apiece annually for some large businesses.

Still, the costs are adding up for companies such as Magma Design Automation Inc., a chip designer in Santa Clara, Calif., which has seen its legal and accounting bills soar. Last quarter, Magma blamed the new rules in shaving a penny off its earnings-per-share -- reporting nine cents instead of 10 cents. The company, which posted $75 million in revenue for fiscal 2003, saw its legal fees jump 105% in the first quarter of 2004.

"We are seeing a significant drain," says Bill Kiernan, Magma's controller. "We would not be doing this level of documentation or going through this extensive an exercise were it not for Sarbanes-Oxley."

Like Magma, most companies say they understand the need for tougher standards but complain that some of the rules are duplicative while others force them to devote thousands of staff hours to formalize procedures already in place. The most pointed criticism is aimed at a rule -- Section 404 of the act -- to improve internal controls over financial reporting. Beginning in June 2004, management at most large companies must have in place tight internal controls, assess the effectiveness of those controls and then pay for an independent assessment by outside auditors.

A survey of 321 companies to be released Tuesday shows that businesses with more than $5 billion in revenue expect to spend an average of $4.7 million each implementing the new 404 rule this year, according to Financial Executives International, which represents top corporate officials. Much of the money is being spent on consultants, lawyers, auditors and new software. Many costs, such as installing

software and designing systems, will decrease after the first year. But other costs are expected to stay constant, including paying an outside auditor to assess the controls every year.

Companies with more than $5 billion in revenue expect those fees to be $1.5 million annually, according to the survey. At World Wrestling Entertainment Inc., management began ramping up internal controls three months ago and is still considering whether to pay $250,000 to hire an outside consultant to oversee the project. The company, which reported revenue of $374 million during fiscal 2003, which ended April 30, already plans to spend about $50,000 on software to help document and track internal-control tests.

It is "a big headache," says Philip Livingston, the company's chief financial officer. "It is a lot of cost to the system without a lot of benefit. It is checking and testing internal controls that are already in place."

Robert Schneider, chief financial officer at Kimball International Inc., a furniture maker in Jasper, Ind., says many of the new rules are beneficial but the work required to document internal controls is an example of the pendulum swinging "too far." Kimball's audit costs are roughly double the $390,000 the company paid in fiscal 2001, Mr. Schneider says. He estimates that the company, which has revenue of about $1.2 billion, will spend about $1.5 million on implementation. Kimball says that spending will include the cost of roughly 16,000 hours that the company estimates employees will spend creating a software system to document internal-controls processes, the cost of its outside audit firm to review that system, as well as the time and effort of internal employees to help the outside auditors.

Company executives say another problem is that while the SEC issued its final internal-controls rule in June, the Public Company Accounting Oversight Board, which regulates the accounting profession, has yet to finalize its rule for how auditors should assess the controls. That is creating uncertainty about audit costs. The oversight board hopes to issue a final standard by the end of March.

Rep. Michael Oxley, the law's co-sponsor, acknowledges that the cost of the internal-controls systems is a burden. "The cost-benefit analysis will always be debated," the Ohio Republican says. But it is "encouraging" that companies already are starting to make disclosures about potential weaknesses, he adds. In the past several months Adecco SA and BearingPoint Inc. disclosed "material weaknesses" in their internal controls.

Douglas Carmichael, the Public Company Accounting Oversight Board's chief auditor, says most companies need to make significant improvements to comply with the rules. "People in the past had a very exaggerated idea of how much time the auditor spent on internal controls," Mr. Carmichael says. "It was viewed by the auditor as strictly an efficiency matter" and auditors "paid little or no attention to internal controls."

One encouraging result of the Financial Executives International survey, according to Mr. Carmichael, is that small companies don't appear to be bearing a disproportionate amount of the cost. Some market observers were worried that increasing costs will dissuade smaller companies from going public. But Mr. Carmichael says small companies may actually benefit from the new requirements, because fraud tends to be more prevalent among small companies, making access to the capital markets harder. The new requirements should reduce uncertainty and therefore improve access, he says.