

UNITED STATES OF AMERICA
THE DEPARTMENT OF THE TREASURY

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ADVISORY COMMITTEE ON
THE AUDITING PROFESSION

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TUESDAY
JULY 22, 2008

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WASHINGTON, D.C.

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The Advisory Committee met in the Cash Room at the headquarters of the US Department of the Treasury, 1500 Pennsylvania Avenue, N.W. Donald T. Nicolaisen and Arthur Levitt, Jr., Co-Chairs, presiding.

MEMBERS PRESENT:

- DONALD T. NICOLAISEN, Co-Chair
- ARTHUR LEVITT, JR., Co-Chair (via telephone)
- ALAN L. BELLER
- MARY K. BUSH
- TIMOTHY P. FLYNN
- ROBERT R. GLAUBER
- KEN GOLDMAN
- GAYLEN R. HANSEN
- BARRY C. MELANCON
- RICHARD H. MURRAY
- GARY JOHN PREVITS
- DAMON SILVERS
- SARAH SMITH (via telephone)
- WILLIAM D. TRAVIS
- PAUL A. VOLCKER
- ANN YERGER

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OBSERVERS PRESENT:

ROBERT HERZ
CONRAD HEWITT
MARK W. OLSON
ZOE-VONNA PALMROSE

TREASURY STAFF PRESENT:

KELLY AYERS
GERRY HUGHES
TIMOTHY HUNT
KRISTEN JACONI
STEVE LAUGHTON

REPORTED BY: CHARLES MORRISON

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P R O C E E D I N G S

(1:04 p.m.)

1
2
3 CO-CHAIR NICOLAISEN: Well, good
4 afternoon. We now have a quorum.
5 Transportation into Washington today is -- has
6 been a problem for just about everybody who's
7 tried to get here.

8 I left New York on the nine o'clock
9 Shuttle and got to Reagan at noon with a
10 diversion to Dulles and threatened return to
11 New York. So, I'm just happy to be here.

12 My Co-Chair, Arthur Levitt, I
13 think, will be joining us by telephone, is not
14 able to get here this afternoon.

15 We have several other Members,
16 mostly due to the weather and traffic and
17 inability to physically be here, who will
18 either join by phone or we'll have to catch up
19 with them later if they're lost in transit.

20 We do have a quorum, so I call the
21 meeting to order. I welcome everybody. I
22 welcome our audience. I welcome those who are

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1 joining us on the webcast.

2 This is an almost-to-the-last
3 session where we'll have an opportunity to
4 have an update as to the status of our report,
5 the work that's been done on it, the things
6 that are particularly noteworthy.

7 And, as has been our practice in
8 the past, we'll ask each of our Subcommittee
9 Chairs to lead the discussion in their area.
10 I would, as always, encourage our observers to
11 participate, to provide your input. All
12 Committee Members are encouraged, if there's
13 any doubt in any way, in any aspect of any of
14 the recommendations that are being made, that
15 you would voice your concern at this point,
16 because we are nearing that point where we
17 will call the report final in the very near
18 term.

19 Sarah, I think, Sarah Smith, you're
20 on the phone.

21 MEMBER SMITH: I am.

22 CO-CHAIR NICOLAISEN: Excellent.

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1 Glad to have you.

2 Chairman Levitt, are you?

3 (No response.)

4 CO-CHAIR NICOLAISEN: No. I think
5 that's it. I think Rodge Cohen will be
6 joining us at some point, as will Rick
7 Simonson, and I assume they will announce
8 themselves as they come on.

9 Today we do not have witnesses
10 before us, so this is the in-house discussion
11 between the Committee and observers, and I
12 think we've made a tremendous amount of
13 progress, and I want to thank everyone for
14 that.

15 I have looked at everyone's
16 comments, as you respond through Kristen, and
17 as you work your way through the document.
18 And I think there's been extremely valuable
19 input that we have.

20 This is getting to be what I think
21 is going to be a very good report on the
22 profession, very good update on the

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1 profession.

2 So, with that, Subcommittee Chair
3 Gary Previts, heading up the human capital
4 section, I will turn it over to you and ask
5 you to lead our discussion.

6 MEMBER PREVITS: Thank you, Don.
7 Good afternoon everyone. I'm pleased to
8 report on behalf of our Subcommittee to bring
9 you up to date on the changes made in the
10 second draft report, which can be relatively
11 quickly highlighted and summarized and then we
12 can open it to questions, and hopefully the
13 hyperbole around these will not be distracting
14 or without purpose.

15 We found that the structure of the
16 recommendations, the five recommendations we
17 have were sound, but were in need of some
18 adjustment to take into consideration items
19 which came to our attention since the drafting
20 of the first round of our human capital
21 section.

22 Among the issues -- and I wanted to

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1 single out Gaylen and Lynn Turner for their
2 particular memo of June 17th. I mentioned it
3 to Gaylen this morning at the CAQ event that
4 it helped sharpen our awareness for the need
5 to take full advantage of what I think Barry
6 calls the law of the land, 150 hour
7 opportunity. And make sure that we put into
8 there more than just hollow hours.

9 And much of what we're facing
10 today, you know, if you go back to when the
11 concept of the additional professional
12 education was added, there were studies such
13 as the one that I'm just taking out of the
14 stack here from one of my dusty shelves.

15 It was done in the early Eighties
16 that, in fact, did study, based on the human
17 resource records of firms, the ability of
18 people with a graduate degree to succeed more
19 rapidly through the exam, to stay longer and
20 be retained longer by the firms, to be
21 promoted more rapidly and so forth.

22 Criteria that we have not really

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1 done a great deal to continue to evaluate over
2 time, in part because firm records aren't
3 always public records. And so, the problem
4 with doing this in a kind of a statistical
5 sampling way doesn't work because you don't
6 have a control group.

7 But, if you do have firm records on
8 HR and you can analyze those -- this isn't
9 just a, you know, an easy question -- it's
10 quite possible to begin to assess the
11 benefits.

12 But that really goes back and begs
13 a question. That was all studied back in the
14 1980s, and so today the opportunity before us
15 is to figure out what it is that we need to do
16 to extract full value from that educational
17 opportunity.

18 Remember that there are, now, a
19 majority of states -- a vast majority of
20 states that require that educational
21 component.

22 That being said, the supply and

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1 demand study is out and it shows, you know,
2 the first study in approximately three years
3 with good information that's, I think,
4 distributed to all the Members.

5 And so, there were a lot of things
6 to chew on as a result of the communications
7 from individuals who submitted material, and
8 with the support of staff, we evaluated and
9 considered and came up with some changes that
10 would amplify the opportunity to reaffirm our
11 expectations that curriculum examinations
12 should capture this high level of educational
13 opportunity which is now the law of the land,
14 and to note that fraud examination, forensic
15 auditing, financial risk management, a number
16 of particulars, would be -- would also be
17 appropriate subject matter.

18 To the extent that it was important
19 to specify it, because technology has been so
20 increasingly important, you know, 20 years ago
21 or 25 years ago to think about the internet
22 was beyond the realm of imagination.

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1 We were in fax machines and bag
2 phones, and so to talk about what it might be
3 in the next decade is, you know, is
4 increasingly challenged, but the need to
5 recognize the benefits of technological
6 innovation and teaching materials was added as
7 a recommendation as well.

8 We spent considerable time talking
9 about the minority representation
10 recommendation, and in particular, to build on
11 the suggestions made by Frank Ross at his last
12 -- at our last meeting when he testified about
13 the importance of mentoring, and the value of
14 having a mentoring program to enhance minority
15 retention.

16 And we also added a footnote item
17 about the issue about the balance comment
18 about qualified individuals who have the
19 opportunity to remain in the country, either,
20 you know, by increasing the current H1-B
21 quota.

22 Now, this was not a position taken

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1 for or against, it was a position that said,
2 this is an issue. So, it's a footnote,
3 Footnote 71.

4 Maybe the best way to leave this is
5 with some perspective on where we are, and
6 thinking about where we need to be. This
7 morning we were treated to the old bromide, if
8 you will, of Wayne Gretzky and skating to
9 where the puck is going to be.

10 Having been in the classroom at
11 Case now for 30 years and been an academic for
12 40 years, I would point out that the next ten
13 years, I think, are going to be by far the
14 most challenging in the last half-century.

15 We are going to see a demographic
16 that's going to affect both the practice
17 community and the academic community in our
18 capacity to -- my best guess -- attempt to
19 double the number of Master's level graduates.

20 To do that without some form of
21 assistance or intervention, if you will, the
22 way that science and medicine has done in the

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1 past, may be particularly challenging.

2 These are personal remarks, not the
3 remarks of the Committee, but I think I owe
4 you an accounting for my best thinking, having
5 been immersed in this project for the last
6 nearly ten months.

7 In the last 30 years the academic
8 community, which I guess I am a representative
9 of, has produced no less than eight score and
10 more schools that have achieved accounting
11 accreditation.

12 The schools that you would
13 recognize the names of, Baylor University,
14 Baruch College, Brigham Young, University of
15 Chicago, University of Southern California,
16 Penn State, Lehigh, William and Mary, Dayton,
17 Notre Dame, Minnesota, Ohio State, Denver,
18 Howard University, Texas at Austin, Georgia,
19 Tennessee, University of Illinois.

20 All of those programs have
21 accredited graduate programs in accounting.
22 They did not exist. The concept of accounting

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1 accreditation did not exist 30 years ago.

2 In those days, if you put out 2000
3 Master's students you would be fortunate.
4 Maybe three. This past year the number was
5 nearly 17,000. And this was done without a
6 dime of federal money.

7 This was done based upon the sweat
8 equity of the campuses of the States, and that
9 challenge faces us, you know, the same kind of
10 challenge, but we don't have to expand by a
11 factor of eight. We only have to expand by a
12 factor of two in ten years.

13 I think that's probably a good bet
14 about, you know, supply capacity that's going
15 to have to be paid attention to, along with
16 all the recommendations.

17 So, I think our recommendations
18 support going forward, giving careful thought
19 to what it will take to create the human
20 capital for the foreseeable future, as is
21 always the case when you have reports of this
22 type. The proof of the pudding will be in the

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1 eating, or will we end up walking the talk?

2 I think the talk is about right. I
3 think we've got the report and the
4 recommendations about right. The ability to
5 deliver on those recommendations will be the
6 major challenge.

7 I want to thank all the Members of
8 the Committee.

9 Sarah, you're over in London this
10 morning, or are you back in the States?

11 MEMBER SMITH: I'm over here.

12 MEMBER PREVITS: Okay. I want to
13 thank every member of the Committee for not
14 ever pulling a punch, for saying what they
15 felt and believed, and oftentimes, although
16 the data was not as compelling or clear as we
17 would have liked for, in good faith, wrestling
18 with the issues and coming out with what I
19 think is a good set of recommendations.

20 And, Barry, I'd invite you, since
21 you're present, and Sarah, if she'd like to
22 comment at all.

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1 MEMBER MELANCON: I think just real
2 quick, I think we tried to take the feedback,
3 as Gary mentioned, and made some
4 modifications. I think it really does reflect
5 where the issue of human capital is today, and
6 with some forward-looking activities, like the
7 study group that's in there for the future.

8 I do think that there are some
9 challenges, but I do think, as you look at the
10 whole landscape of the demographics of
11 society, the profession actually has a leg up
12 in winning that. It's just a matter of how it
13 progresses over the next couple of years.

14 MEMBER PREVITS: Sarah, any
15 comments?

16 MEMBER SMITH: Gary, I just wanted
17 to mention that we did not ignore the several
18 comments that came through from people who
19 responded, the subject of addressing women in
20 the profession.

21 And what we did, in looking at the
22 data, we felt that putting the actual

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1 statistics in the footnotes to the report
2 would be helpful in explaining our thinking,
3 which was that entry level is very healthy and
4 over the last few years we've seen
5 improvements each time the statistics have
6 been done in terms of partnership and some
7 more senior rank for women.

8 So, I didn't want people to think
9 that we didn't look at that, nor do we not
10 think it's important. We do think it's very
11 important, but since the profession seems to
12 be making strides, although, you know,
13 possibly not as fast as we would want, that we
14 felt putting in the statistics would help
15 people see that.

16 MEMBER PREVITS: Don, I suspect
17 that we've heard the feedback from the
18 Committee Members. I'll perhaps turn it back
19 to you for questions or however you care to
20 proceed.

21 CO-CHAIR NICOLAISEN: Great. Thank
22 you very much. Any comments, suggestions,

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1 recommendations, questions, concerns?
2 Anything that this Subcommittee has missed
3 that you would have anticipated they would
4 have dealt with?

5 MEMBER VOLCKER: What do you mean,
6 human resources?

7 CO-CHAIR NICOLAISEN: Human
8 resources.

9 MEMBER VOLCKER: Let me make a
10 comment which may or not qualifying --

11 CO-CHAIR NICOLAISEN: Right there.
12 This little button.

13 MEMBER VOLCKER: Maybe a little
14 late, but when I read this it all sounded, you
15 know, competent, interesting, but it missed
16 what I feel.

17 The more I'm involved with
18 accounting, the more I realize how difficult
19 it is and the importance of it, and I don't
20 think it receives sufficient attention in a
21 lot of respects.

22 The profession doesn't have the

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1 prestige it should have. I don't think it
2 attracts the talent that it should, and one
3 reflection of that is I think -- my
4 impression, anyway, is the most prestigious
5 universities and business schools don't even
6 teach it, but they don't teach it as a
7 separate subject, anyway. They touch upon it.

8 And shouldn't we say something
9 about this, that you know, the profession is
10 neglected, and it's not attracting the talent
11 that it should. I read a lot of stuff here
12 about education, broadening the education.

13 That's fine, but I don't think it
14 quite gets to the point that, you know, the
15 whole level of the profession ought to be
16 raised in the public eye and in the eye of, I
17 suspect, of accountants, themselves, to a
18 considerable extent, because it really is a
19 subject worthy of a lot of intellectual
20 effort.

21 CO-CHAIR NICOLAISEN: Let me --
22 I'll let Gary comment in more detail, but this

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1 had been very early on in the dialogue of the
2 whole Committee, that had been observed, had
3 been considered as a -- as a significant
4 concern.

5 And I think that in the background
6 of what will surface in other parts of this
7 report, which are not yet complete, not yet
8 drafted -- perhaps is a better term -- there
9 will be a background section and it will also
10 be a report of the Chairman, and in that area
11 I think you can rest assured that we will have
12 commentary to that effect.

13 I'm not sure that the solutions are
14 necessarily easy. They certainly are long-
15 term, and it won't be an on/off switch, but
16 that has -- your observations are exactly
17 right, and I think it's a concern that is
18 shared, probably by every Member of this
19 Committee, and I see our observers nodding
20 their heads yes as well.

21 So, we do need to deal with that.
22 And I thank you for that input.

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1 Gary.

2 MEMBER PREVITS: Mr. Chairman, I
3 appreciate the observation about prestige. I
4 think that's -- you couldn't find a more
5 hearty supporter of that concern in terms of
6 the public image that we have and what we
7 would need to have to carry the kind of
8 support, I think, it's going to require to
9 have the interventions to develop the capacity
10 that would serve society at the highest
11 levels, because I think the resource question
12 about our capacity to educate people properly
13 for the coming years is a clear and difficult
14 challenge.

15 As far as getting into 'tis/'taint
16 about which campuses do and which campuses
17 don't, I think before you walked in I had
18 mentioned the accredited programs in
19 accounting which go from very good schools,
20 including the University of Chicago to
21 Southern Cal, to all the -- most all the so-
22 called Big Ten schools that have, I mean, I

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1 think good research reputations.

2 It's true that perhaps, you know,
3 some of them -- these were the accredited
4 schools. There are still programs at Wharton,
5 for example, that have not gone the
6 accreditation route, but they still have very
7 strong accounting programs.

8 So, I'd be less concerned about --
9 I think the word you used was neglected --
10 neglected at prestigious institutions. The
11 president of our National Association, the
12 American Accounting Association, last year is
13 a professor at Yale.

14 Now, he calls himself a professor
15 of economics, finance and accounting, so it's
16 a different kind of, you know, caricature, but
17 his interests are clearly in the financial
18 reporting area.

19 And I think when you get to
20 institutions in the Ivy's, maybe in that
21 regard you're right, it's probably in the
22 underrepresented. But from a popular point of

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1 view of high-quality schools through the
2 country that have achieved accounting
3 accreditation, the record is clear.

4 Over 160 schools have paid that
5 price from the most notable to some that are
6 maybe less notable. So, you know, I wouldn't
7 hang a lot on the neglect at the prestige
8 campuses, although I think that probably does
9 count for a lot in certain circles.

10 The matter of the reputation of the
11 firm -- of the profession and its public
12 prestige, I agree. We have an issue.

13 CO-CHAIR NICOLAISEN: Rick?

14 MEMBER MURRAY: Thank you. I also
15 agree with and appreciate Chairman Volcker's
16 observations about the prestige challenge that
17 is faced here.

18 Having watched or been involved in
19 the profession for 40 years, it seems to me
20 that we've gone through an enormous growth in
21 competencies, but not a similar growth in
22 stature relative to peer groups that one might

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1 measure in terms of attracting people into the
2 profession.

3 My only concern is what we do with
4 that observation, because it's one of those
5 clearly evident truths, the articulation of
6 which may make the solution more difficult to
7 achieve than if we didn't quite say this is a
8 profession that suffers from a lack of wide
9 appreciation or sufficient attention at
10 premier universities.

11 Otherwise, having made no
12 contribution at all to this subject, I would
13 like to thank Gary and his Subcommittee for
14 what I think is an extremely thoughtful and
15 valuable contribution to the Committee's work.

16 CO-CHAIR NICOLAISEN: Thank you,
17 Rick.

18 I think the context in which all of
19 us are addressing this is that the audit
20 profession is critically important to an
21 orderly and fair society, that they play a
22 role that's unique, that it's highly valued

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1 and that perhaps that -- just that aspect
2 hasn't been adequately communicated, either.

3 So, I think you'll -- I think we do
4 have a delicate task to complete, but I would
5 hope that if this Committee is known for
6 nothing else, that we would come across as
7 having reemphasized and stressed the
8 importance to our capital markets of a very
9 competent, strong audit profession.

10 And it gets back to the very
11 reasons why Secretary Paulson chose to create
12 this group and, you know, I think we're
13 beginning to make some progress, but we will -
14 - we'll put our effort into it.

15 Gaylen.

16 MEMBER HANSEN: Thank you, and I'd
17 like to thank Gary for your Subcommittee's
18 hard work on this.

19 I have raised, I think, at least in
20 the draft, the question about the gender
21 issue, and maybe you could comment on that.
22 You know, when I graduated from college -- and

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1 it wasn't 40 years ago -- it was 30 years ago,
2 so I don't have as much experience as Rick
3 does here, but there were four of us and we
4 were all interns for the same firm from my
5 school and there were two men, two women.

6 And I thought all four -- I thought
7 things were balanced because of that. And
8 then I found out that they weren't quite so
9 balanced.

10 And over, you know, that 30-year
11 period, I think they have come into more
12 balance, but just the fact that I don't know
13 that there's any CPA's on this Committee that
14 are women -- representing women.

15 I just wondered if it isn't worth
16 at least a comment. The importance that women
17 play in the workplace, the flexible week
18 schedule or working schedules that they have
19 to deal with, do they have a track-to-partner
20 in the firms that -- isn't any comment along
21 those lines.

22 And I realize, you know, some

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1 people might question whether women are a
2 minority, depending upon your political
3 persuasion. Irrespective of that, I just -- I
4 just think they play such a critical role and
5 I work with so many of them that are
6 tremendously talented and competent, I wonder
7 if it shouldn't be addressed.

8 MEMBER MELANCON: I'll take that
9 one, Don.

10 And I know Sarah is on the phone,
11 but I think the summary of the -- we had three
12 women on the Subcommittee and we discussed
13 this at considerable length.

14 I think all of those issues that
15 you described about work-life balance issues
16 which, by the way, you could make the same
17 argument on a generational sense, not even on
18 a male-versus-female sense.

19 It crosses all business and
20 profession and industry issues, point number
21 one. And I think we felt that, in fact,
22 there's a lot of evidence that the profession

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1 does a better job than many others in doing
2 that.

3 If you look at lists that are
4 published by commercial enterprises of best
5 places to work and things of that nature, the
6 profession -- not just the Big Four, by the
7 way, many different size firms do very, very
8 well on that list.

9 Secondly, we just published a
10 report that shows the highest number of female
11 partners in CPA firms in history, at 23
12 percent. That number will continue to grow.
13 It's an evolution of greater than 50 percent
14 of the entry class of CPAs being female for
15 several years now, and the normal
16 matriculation process to the partner level
17 from a public accounting perspective.

18 That's not to diminish in any way
19 the CPAs who -- female CPAs who have very
20 significant roles in business and industry and
21 in finance functions and otherwise.

22 And we did put that, as Sarah

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1 mentioned in her comments, we did put that,
2 and referenced that in a footnote because it
3 was raised, Gaylen, as you said, and it was
4 raised at the last meeting, and the
5 Subcommittee wanted to reflect the fact that
6 we had considered it. We put it in the
7 footnote to acknowledge that that progress is
8 there.

9 But that was the thinking of the
10 Committee from that standpoint. The points
11 all being very, very important, but
12 essentially the progress is clearly there.
13 The numbers that are record numbers, and some
14 of the issues and challenges that you
15 described are not unique to this profession.
16 They are, in fact, -- they cut across all
17 industries and all professions.

18 MEMBER SMITH: And just to second
19 that, Barry, the fact that work-life balance
20 has been talked of, in terms of both genders
21 now.

22 It's really very critical to those

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1 of us who have been or are in the profession.

2 We think that's a very important point. We
3 don't want to make that a female issue. I
4 think that does not do well for us long-term.

5 CO-CHAIR NICOLAISEN: Gary, maybe
6 it is worth taking a look one more time at the
7 wording that's in the report around this, and
8 I'm sure you're confident that -- that we've
9 done that, but there is a sensitivity out
10 there that perhaps we may not have fully
11 captured, I think, the spirit of the
12 Subcommittee.

13 And certainly the spirit of this
14 Committee has been that we would like to see
15 that representation continue, and I believe
16 the firms are confident that they've been
17 taking the steps to ensure that that happens.

18 Maybe we haven't -- maybe we can
19 elaborate a little bit more in the report on
20 that.

21 MEMBER PREVITS: I was just going
22 to comment before Tim gets in on the

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1 conversation, that we also are walking a fine
2 line here in minority representation in our
3 focus on that Recommendation, and so, you
4 know, we are very sensitive to having the
5 correct language in place.

6 I think we've got it right in the
7 new note, number 17, that we've added to the
8 report, but we'll take another look at it.

9 CO-CHAIR NICOLAISEN: Great. Thank
10 you very much. Ken, I think you were next,
11 and then Tim.

12 MEMBER GOLDMAN: Yes. I want to
13 actually possibly comment, follow up to a
14 comment that Chairman Volcker was saying.

15 And it comes back to -- I think
16 about when I, myself, when I learned
17 accounting, and I sort of watched what's going
18 on in terms of the subprime fiasco, the
19 mortgage fiasco and everything there.

20 And one of the things I have been
21 suggesting, and it's hard to get pushed
22 through, because I've been involved in an high

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1 school endeavor, is the thought of financial
2 literacy or lack thereof that starts really in
3 high school and college, which really accounts
4 for two things.

5 One is, folks don't take
6 responsibility for their own finances because
7 they don't understand them. And two is, you
8 talk about the, you know, profession, and
9 people having more dignity and so forth in the
10 profession, and part of it is, I think, would
11 be helped if we had a better familiarity with
12 the profession early on.

13 So, I don't know if it's really
14 part of the province of any of our
15 Subcommittees, but it just strikes me, as you
16 walk around and you see what's going on in the
17 environment today, and then you see what we're
18 trying to accomplish here, that a lot of it
19 starts with just the lack of understanding of
20 basic financial concepts, understanding your
21 net worth, understanding how to take care of
22 your own self as opposed to quote, unquote,

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1 blaming it on someone else.

2 So, I don't know how to put that in
3 words, but it just strikes me that's sort of -
4 - that's where really a lot of the issues
5 start.

6 CO-CHAIR NICOLAISEN: Right. Thank
7 you. I know Barry probably feels like a lot
8 of what the AICPA has done over the years
9 doesn't necessarily get recognized, but I know
10 that there has been -- there have been many
11 campaigns to do exactly what you have
12 described and an awful lot of people actively
13 involved in it.

14 The question is: how do you get
15 broader exposure, perhaps, to ensure that --
16 that it not only happens, but people respond.

17 MEMBER GOLDMAN: Well, I just
18 think, if I could add one thing, I just think
19 part of it is to suggest strong enough, which
20 hasn't always been successful, that high
21 schools start teaching a basic course in
22 accounting of some form or another, make it

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1 simple, whatever, if you have to, but you
2 start there.

3 So, when you come out of high
4 school you have some knowledge of handling
5 your own financial affairs.

6 CO-CHAIR NICOLAISEN: Good. Thank
7 you.

8 Barry, I know you were anxious to -
9 -

10 MEMBER MELANCON: No, I won't go
11 into a lot of detail. There is, just for your
12 information, a Presidential Commission on
13 Financial Literacy along the lines of which
14 you have just said, Ken, that I hope that --
15 this Administration hopes survives multiple
16 administrations similar to when we were all
17 growing up with the Presidential Commission on
18 Physical Fitness, so there is a major push in
19 this -- in this town, and in government for
20 that, of which the profession is a very key
21 player in it.

22 I would commend you to

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1 360degreesoffinancialliteracy.org, which is a
2 major push of the profession's investment
3 along those lines.

4 But to your high school point, I
5 know you were talking about it from a general
6 business knowledge perspective. There is a
7 fair amount of evidence that actually shows
8 that, believe it or not, a person majoring in
9 accounting, ultimately becoming an accountant
10 -- and I know your point was general
11 knowledge, but if they go to a high school
12 that has an accounting course in high school,
13 they are actually less likely to major in
14 accounting.

15 So -- and we have some pretty hard
16 evidence on that. So, it's -- I think what
17 you -- if I could just amend your words, I
18 think there's a general business awareness as
19 opposed to accounting, financial literacy-type
20 courses, and you will be happy to know that
21 there are some states that are actually --
22 and we are supportive of that through the

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1 CPA's societies, et cetera.

2 There are obviously costs
3 associated with adding curricula in high
4 schools, but there are some states that are
5 embedding that into the high school
6 curriculum.

7 Again, not accounting, per se, but
8 the financial literacy point that you
9 described, and there are a lot of programs
10 like HeadStart and others that are focused on
11 that. JumpStart, excuse me.

12 CO-CHAIR NICOLAISEN: Great. Thank
13 you. Tim Flynn.

14 MEMBER FLYNN: I did take
15 accounting in high school, so I don't know
16 what that says for me, Barry, but -- and I'm
17 glad I did.

18 I think the report is very well
19 done. I just have a couple of observations
20 and may tie back into what we've been talking
21 about a few moments.

22 One, I think maybe up front is the

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1 chance to celebrate some of the profession's
2 success in the forefront of this dialogue. I
3 think if we look at the gender issue and the
4 dialogue around that, we've made tremendous
5 progress as a profession in the last ten years
6 on a gender basis.

7 We've focused on it. The retention
8 -- for the first time in my firm's history,
9 retention of our female management group is
10 higher than our male management group, with
11 18.5 percent or so women partners, up from,
12 you know, single digits seven years ago, and
13 the profession on a whole is in high teens.

14 So, there's tremendous things
15 happening, and the evidence there is that
16 we've focused on it. We've looked at it.
17 We've created environments, and there's been
18 great progress.

19 I think that can draw an analogy
20 to, from the standpoint of the other diversity
21 we're talking about in the document, that if
22 by focusing on it and driving that we can have

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1 the same type of success, by not taking our
2 foot off the pedal on the gender side, but
3 taking that momentum into the minority side
4 and other parts of diversity.

5 So, I think that could be very well
6 -- and I think the point that Barry made, we
7 should celebrate a little bit. I don't know
8 how many other professions, the top four size
9 firms, at least in our profession, are all in
10 the great places to work for Fortune.

11 All four firms are a great place to
12 launch your career in Business Week. We're
13 represented, all firms, in Working Mother,
14 Diversity lists. I mean, there is tremendous
15 focus on the work place, and we have a lot of
16 really talented, smart people. A lot of
17 really talented, smart people.

18 Can we improve? Yes. Can we get
19 more business schools involved? Yes.
20 Advanced degrees? Yes.

21 But I think a little bit of
22 celebration of the talent in the profession

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1 today doing the complex issues might be a way
2 to lean on this a little bit in the forepart
3 of the document.

4 MEMBER PREVITS: You will never
5 find me opposing a party anywhere, Tim.

6 MEMBER FLYNN: That's not just the
7 top four firms.

8 MEMBER MELANCON: Well, I just said
9 that Tim is absolutely correct. I agree with
10 what he said, but just, when you look at those
11 lists, it goes beyond the four firms as well,
12 so I think it's culturally in a lot of
13 different places in the firm.

14 MEMBER FLYNN: I agree, Barry, but
15 my point, I think, a little bit is that's very
16 important and celebrate all that, but if you
17 look at just the pure size of the profession
18 that's represented on that list, just the pure
19 numbers on that list and take any other
20 industry or profession, it's incredible.

21 MEMBER MELANCON: I agree.

22 MEMBER FLYNN: And I think that's

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1 the part that we have to leverage off of.

2 CO-CHAIR NICOLAISEN: Great. I
3 think that's really good input and probably
4 does deserve a section in maybe a few charts
5 and graphs as well in the document.

6 It's one of the things that always
7 happens with any Committee that studies
8 something, you tend to look at the things that
9 aren't working and you don't always talk about
10 all the things that are working very well.

11 And we probably -- we probably can
12 all go through this and do a little reflecting
13 on do we have the right balance in the entire
14 document.

15 I think this has been a very
16 healthy discussion.

17 Bob, did you -- okay. Mark.

18 MR. OLSON: You may have just
19 wrapped up the topic, and maybe I shouldn't
20 offer this, but the concern I have is that if
21 we were to pursue the idea of the accounting
22 profession being respected, that strikes me as

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1 a fairly ethereal goal.

2 I'm not sure that you can achieve
3 respect. And I think that respect is
4 conferred. And as I -- if we were to stand out
5 and say, our goal is to become respected, I
6 think you would have -- that would be the end
7 result of a lot of the components I think that
8 Tim just talked about.

9 The recognition of the quality of
10 the work experience, the value of that work
11 experience to society. If I look at -- if I
12 look at professions that I think of as being
13 prestigious, for example, in the medical
14 profession, there are certain elements of the
15 medical profession that are thought to be
16 prestigious, but they are at a higher level.
17 They are at a higher education level or that
18 there has been a significant winnowing process
19 with the people that get there.

20 I don't think of -- I don't hear
21 the law profession being generally described
22 as prestigious, although -- although I think

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1 of the people who are judges, for example,
2 are, so -- in the winnowing.

3 So, I think in order to achieve
4 prestige, I think we would almost have to
5 stratify the profession in a way that would --
6 that I think is inconsistent with the goal of
7 this Committee.

8 And so, I would be -- I would much
9 -- I think that the emphasis ought to be on
10 the contribution of the profession and the
11 value of the profession to both financial
12 reporting and broadly, more broadly to the
13 societal value.

14 CO-CHAIR NICOLAISEN: Right. Thank
15 you, Mark.

16 I think Bob Herz said it in one of
17 the very first meetings, that there aren't too
18 many television programs or movies about CPAs,
19 and he, I don't think, has had any movie
20 contracts as Chairman of the FASB in the
21 interim period, but if anyone has a
22 recommendation as to who might play a starring

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1 role, we certainly will entertain ways to get
2 that in the document.

3 Thank you. I think it's been a
4 very good discussion of human capital. Gary,
5 thank you very much. Thank your Subcommittee
6 very much for all of your efforts.

7 Let's turn next to Bob Glauber and
8 Bob has had not the easiest Subcommittee
9 issues to deal with. He's been dealing with
10 firm structure and finances and many other
11 things attendant to that.

12 If you would, would you please
13 update the rest of the Committee on your
14 progress.

15 MEMBER GLAUBER: Certainly. The
16 issues may make it difficult, but I am most
17 fortunate to have the Subcommittee I do, and I
18 want to again say how fortunate I think I am
19 to have been asked to chair the Subcommittee,
20 composed as it is of such wise and
21 knowledgeable people with diverse and
22 strongly-held positions.

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1 Let me do several things. First,
2 let me update you and call your attention to
3 the major changes in this draft as compared
4 with the previous one.

5 And then what I'm going to do, one
6 of our members is unable, because of
7 scheduling conflicts, Lynn Turner, to be with
8 us, and I did tell him that I would -- I asked
9 him for a summary. I asked him for a summary
10 of his positions that differ from -- in
11 important ways from the Subcommittee's current
12 draft, and I just told him I would present
13 those to you.

14 For a list of the ways in which the
15 Subcommittee's recommendations differ
16 importantly from the previous draft, the first
17 is in Recommendation 1, which centers on the
18 creation of a national fraud center.

19 And you will note in the
20 Recommendation there is a bracketed space. We
21 are inviting applicants to lead in the
22 creation of a national fraud detection center.

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1 It's difficult to get the right
2 person or group to do this. And we've, at one
3 time or another, had several nominees, some
4 which I think ultimately the Subcommittee felt
5 was not just the right balance, some who
6 declined the nomination.

7 So, we are at this point without
8 anybody. We're going to continue to approach
9 proper groups to see if we can't put in this
10 recommendation a formal named entity.

11 Recommendation 2(a) which deals
12 with the UAA's mobility provisions, I just
13 want to make sure that you see that this now
14 clarifies that our call for congressional
15 legislation with a federal provision requiring
16 states to adopt the UAA's mobility provisions
17 would only apply to those states that have not
18 already adopted those provisions.

19 It also -- this Recommendation also
20 now updates the numbers on the number of
21 states that have adopted these provisions.
22 It's now up to 31 states.

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1 Recommendation 5, which is the
2 auditor's report, we have essentially combined
3 our old Recommendation 5 and Recommendation
4 1(b), which also dealt with the auditor's role
5 in fraud detection and made them into a single
6 recommendation which deals with improving the
7 auditor's reporting model.

8 Recommendation 6, we now recommend
9 that the PCAOB will be -- undertake a
10 standard-setting initiative to consider
11 mandating the engagement partner's signature
12 on the auditor's report.

13 We had put that possible provision
14 out for comment in the last draft and, indeed,
15 we have adopted that now.

16 And then finally Recommendation 7
17 on transparency reporting, we recommend that
18 firms file an audited financial statement with
19 the PCAOB on a confidential basis beginning in
20 2011.

21 In addition, as we have before, we
22 recommend that the firms file a public report,

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1 including a report similar to the EU-40 --
2 Article 40 transparency report, and other
3 audit quality indicators as recommended by the
4 Subcommittee on Concentration and Competition.

5 What you will note, and we again
6 put this out for comment, in this
7 recommendation we simply leave it at
8 recommending that these audited financial
9 statements be filed with the PCAOB.

10 What is not in this draft, which I
11 should point out to you is any recommendation
12 on litigation reform. Again, in the earlier
13 draft we said we were putting out for further
14 discussion some possible idea on litigation
15 reform.

16 What I have to report to you is
17 that the Subcommittee is unable to reach a
18 consensus on any meaningful and actionable
19 litigation reform recommendation.

20 We have worked, I think, very hard
21 with the encouragement of the chairs of the
22 Committee and really, the committed attention

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1 of the Subcommittee, and their indulgence in a
2 number of meetings, but we just have been
3 unable to reach consensus on what would be a
4 meaningful and actionable litigation reform
5 recommendation; the views just really are
6 quite disparate.

7 After further talk with the senior
8 management of the Committee, I have agreed
9 that the best way for us to try to proceed
10 from here is to produce a fair and balanced
11 statement by the Subcommittee of the various
12 views on litigation reform and the issues
13 surrounding litigation reform.

14 And we are working on that. I hope
15 we will have a success. We plan to convene
16 another meeting of the Subcommittee at which
17 we will discuss this further, and I hope to be
18 able to present to you such a statement.

19 It would be a statement of the
20 differing views on the range of these issues
21 surrounding litigation reform, and to do it in
22 a balanced way that left the entire

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1 Subcommittee comfortable as to its
2 presentation.

3 So that's where we are. Just for
4 completeness, as I said I would before, let me
5 just note on behalf of Lynn Turner, who is
6 unable to attend today's meetings, sort of the
7 -- his major points of disagreement with the
8 current chapter draft.

9 On Recommendation 1, he would
10 oppose, and indeed in part because of his
11 opposition, we have taken out the Center for
12 Audit Quality as the lead in forming this
13 national fraud center.

14 Furthermore, he does not believe
15 fraud detection best practices will be of much
16 help.

17 On Recommendation 3, auditing firm
18 governance, he believes that the
19 recommendation should require a majority of
20 independent board members.

21 Currently, the Recommendation
22 doesn't specify any number of independent

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1 board members, but he does recommend that
2 there be independent board members on the
3 boards of the large auditing firms.

4 He believes that this governance
5 change should be, quote, accomplished without
6 requiring significant changes to either the
7 independence requirements or the liability
8 regimes of the firms, that is, in particular,
9 adding independent board members.

10 And we've had some discussion of
11 whether it will be possible to do that in the
12 context of the current liability regime facing
13 the firms.

14 As regard to Recommendation 5, the
15 auditor's report, he disagrees with the
16 following statement in this Recommendation.
17 Some say the public -- this is a quote in the
18 Recommendation -- some say the public may
19 believe that auditors will detect more fraud
20 than those in the profession believe can be
21 reasonably expected. He disagrees with that
22 statement.

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1 And then finally, on transparency
2 reporting, he believes audited financial
3 statements should be made available to the
4 public, and particularly audit committees and
5 investors.

6 So, Mr. Chairman, that is a summary
7 of his positions, and indeed, a summary of the
8 changes in this draft of the Subcommittee's
9 chapter.

10 Perhaps other members of the
11 Subcommittee would like to make some comments.

12 CO-CHAIR NICOLAISEN: Rick, would
13 you --

14 MEMBER MURRAY: Thank you, Bob.

15 Your generous comment about the
16 Committee requires a rebuttal that the
17 Committee's good humor and good health has
18 depended entirely on your ability to keep us
19 capable of that state of affairs, Bob. Thank
20 you for your leadership.

21 Just a few basic observations about
22 what we have not yet been able to agree on in

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1 respect of the liability issues.

2 I think it is clear that, despite
3 an extraordinary amount of time and effort and
4 leadership on Bob's part, we are unable to
5 agree as to whether or not there is a
6 sustainability hazard to the business model of
7 the large public company audit firms that
8 compels remediation in some form in the public
9 and capital markets' interests.

10 And I don't anticipate that the
11 remaining time and opportunity for
12 contemplation is going to change that
13 difficulty.

14 There has been a second issue that
15 I think needs to be acknowledged as an
16 impasse, in fact, and that reflects the work
17 of the Subcommittee as to the extent that
18 there is a general recognition that liability
19 is at least an annoying -- annoyingly
20 troublesome fact of life for the large firms.

21 We have a difference of view that
22 has not been fully reconciled as to whether

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1 the cause of that condition is primarily a
2 failure of audit quality or whether it is a
3 condition also heavily and inevitably
4 influenced by the intrinsic burdens of bearing
5 the responsibilities of public company
6 auditing in the economic conditions that we're
7 dealing with today.

8 Recognizing those impasses, I think
9 is a necessary conclusion and one that we
10 ought to deal with openly and candidly.

11 I agree with and support the
12 recommendations that have been made. I
13 believe they're sound. I believe there may
14 need to be some observations added at the end
15 of the day as to where those Recommendations
16 may aggravate the liability problems for those
17 of us who are concerned about them.

18 And when the report is put together
19 as a full Committee report, I think it will be
20 important that we find the way to avoid
21 creating the impression that the collective
22 recommendations of our Subcommittee and the

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1 other Subcommittees are accepted by the
2 Committee as a whole as being effective
3 remediations of the problem.

4 I think this is -- the fault line
5 we have not been able to close within our
6 Subcommittee is a fault line that needs to be
7 recognized as part of the full Committee's
8 report, and in that respect there is -- there
9 are a few elements of the language in the
10 competition section that bear upon the same
11 issues that I've just identified as
12 irreconcilable by us that here or before the
13 issue is -- the report is issued, need to be
14 reconciled so that we aren't appearing to be
15 saying two different things in the same
16 report.

17 CO-CHAIR NICOLAISEN: Good. Thank
18 you, Rick.

19 Gaylen.

20 MEMBER HANSEN: Bob, thank you, and
21 you had said that -- this goes to a
22 Recommendation number 1 and the fraud center

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1 and applications, and I've -- actually, when I
2 was reading through this I wondered who that
3 bracket was that was going to head that up.

4 But, early in the discussions when
5 this came along, NASBA was one of the names
6 that was thrown out there, and that's not
7 something that NASBA has campaigned for.

8 They do have a subsidiary called
9 the Center for Public Trust, and I've been
10 wondering about whether that would fit in
11 their, you know, their mission statement and
12 their background.

13 I discussed that with the NASBA
14 leadership over the last couple of days, and
15 despite not campaigning for it, I think that's
16 something that they would enthusiastically
17 entertain, and so I think that is a
18 possibility if you'd maybe -- maybe want to
19 consider and talk to the folks at NASBA, I
20 being one of them, but I think that is a
21 possibility.

22 CO-CHAIR NICOLAISEN: Right. For

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1 those who may be listening on the web, NASBA
2 is --

3 MEMBER HANSEN: The National
4 Association of State Boards of Accountancy.

5 CO-CHAIR NICOLAISEN: Right. Thank
6 you. Which is a very large group.

7 Any other comments, observations,
8 recommendations?

9 Bill?

10 MEMBER TRAVIS: Thanks, Don. I'd
11 like to throw my hat in the ring and thank Bob
12 for his yeoman's job on a very challenging and
13 frustrating, at times, discussion.

14 I want to focus my remarks on the
15 litigation environment. It's been a difficult
16 discussion for us, and so I went back to the
17 early remarks of Secretary Paulson about the
18 purpose of this Advisory Committee and some of
19 the reasons for the Advisory Committee. And
20 he highlights some things that I think are
21 important to bring to bear.

22 One of those things is he commented

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1 early on about his concern about the
2 litigation environment in the US, and as you
3 can see from our particular set of
4 recommendations, the litigation environment
5 hits in more than one place.

6 I think the firms generally agree
7 that having independent directors in their
8 organizations would be a plus. However, as
9 we've discussed in our Subcommittee, the
10 ability to attract anyone to those roles is
11 highly tied to the ability to obtain insurance
12 or to protect themselves in a litigious
13 environment.

14 Another recommendation has to do
15 with the disclosure of audited financial
16 statements, and one of the key objections that
17 the firms have raised is not necessarily just
18 relevance of the information, but the
19 increased litigation risk that would result
20 from having that information be public when
21 it's not readily available to the plaintiffs'
22 bar, plaintiffs' attorneys at this point in

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1 time.

2 And, as we've discussed in a
3 variety of scenarios, is there a challenge to
4 the long-term global competitiveness of the US
5 environment, and the ability of globalizing
6 the US audit firms -- or the audit firms
7 because of the litigious environment in the
8 US.

9 So, I think it's critical that we
10 address this issue. In my opinion it would be
11 unconscionable not to address the issue
12 because I think it's been fairly clearly
13 stated that the loss of one of the major four
14 firms would be a serious, if not catastrophic,
15 blow to the US capital markets.

16 I think the risk of that loss is
17 significant enough because of the impact, that
18 we need to take this very seriously and we
19 need to get the two sides together to agree on
20 the facts and agree on a solution that makes
21 some sense.

22 Because, to simply say the elephant

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1 is in the room and we can't agree on whether
2 it's an elephant or a really large rhinoceros
3 makes no sense.

4 I think we absolutely have to get
5 together to come up with a recommendation on
6 behalf of the US capital markets that does
7 make sense so that we protect the interests of
8 our economy and protect the interest of a very
9 important profession as it relates to
10 protecting investors.

11 CPA firms have a lot of work to do
12 to continue to build their trust and respect.
13 I agree with the comments earlier, it's not
14 something that is given, it is something that
15 is earned.

16 It's much like a brand. You can
17 market all you want, but ultimately it's your
18 actions that will determine whether you
19 deserve the brand you get.

20 And so, I think the firms have made
21 a lot of progress. I think transparency on
22 what the firms are up to is really, really

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1 important to go to build trust in the firms,
2 but I also think getting to the table with the
3 two disparate sides and coming up with a
4 recommendation is something we have to do.

5 Thank you.

6 CO-CHAIR NICOLAISEN: Ann.

7 MEMBER YERGER: I don't want to
8 have a repeat of a Subcommittee meeting, so
9 let me just first of all say to the record,
10 Bob, thank you very much. I know this has
11 been difficult and I think it's really a
12 compliment to the Treasury Department that
13 they've created such a diverse Committee with
14 individuals with very diverse opinions on very
15 important issues.

16 I think that I am comfortable with
17 the direction that the Subcommittee is headed
18 with this statement. With all due respect, I
19 just don't think the two sides are going to be
20 able to bridge what I see as a huge gulf.

21 I think there is a very sincere
22 difference of opinion about whether the data

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1 provided supports a public policy
2 recommendation that would somehow change the
3 liability regime that's covering the audit
4 profession versus other organizations in our
5 securities litigation environment.

6 And that is really where we are.
7 So, I want to thank you, Bob, and I'd like to
8 thank all the Committee members. I know this
9 has been a difficult issue, but personally I
10 think that we are now headed in the right
11 direction on this.

12 CO-CHAIR NICOLAISEN: Ann, thank
13 you.

14 Tim.

15 MEMBER FLYNN: Thank you. I guess
16 I'll throw my weight toward Bob and his
17 leadership as well. I'm not sure anybody
18 could have navigated us through like he did,
19 because they have been very spirited and, I
20 think, meaningful discussions, and I think it
21 does represent the balance of the Committee
22 and the views, and I think that's what makes

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1 our capital markets work and everything else,
2 is to have these kind of debates and put forth
3 our strong intentions.

4 Ultimately, though, I think this
5 will be a policy issue. I think Alan Beller's
6 comments at the last meeting were very much on
7 point. The world is globalizing. The
8 regulatory environment is globalizing. The
9 accounting standards, the accounting
10 literature is globalizing and the firms are
11 globalizing.

12 Why? Because the capital markets
13 are globalizing, and there's been a tremendous
14 shift in capital markets in the last couple of
15 years, and those flows are going to continue
16 to change.

17 And there could be a time when it's
18 everybody else in the firms together except
19 for the US, as Alan talked about, and that is
20 a real issue and a real possibility, and that
21 would not be a good thing for the profession
22 or the capital markets.

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1 So, I believe it's important for us
2 to set forth the arguments on both sides. I
3 don't think we're going to get to a
4 resolution, and I respect that, but I think we
5 owe it to ourselves to come forward with both
6 arguments and challenge this debate to stay in
7 the forefront and keep it alive, because the
8 world's going to globalize around us and this
9 issue has to be dealt with.

10 And I'm confident that if we can
11 set the right tone and get the right facts out
12 there that we can continue this journey and
13 debate together and we can see it two and
14 three years from now, and we will look
15 different than we do today.

16 I'm convinced of that, and I think
17 the EU and what they're doing, you know, and
18 the other parts of the world will drive us to
19 that point over time.

20 And so I would encourage us to come
21 together for that last phone call to bring
22 forward the balanced point of views and to

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1 make sure that we challenge the capital market
2 system collectively, not to lose this debate.

3 This is very important for the
4 profession, but I think equally important for
5 the capital market system in the US as well.

6 CO-CHAIR NICOLAISEN: Thank you. I
7 think it is difficult for people who are used
8 to -- which is this entire Committee -- used
9 to taking decisions and then having actions
10 occur as a result.

11 It is difficult to say we can't
12 reach that point. I am convinced, though, we
13 have reached that point and I have sat in on
14 enough of the Subcommittee's deliberations and
15 have had enough conversations with others to
16 appreciate that this is a gulf that is pretty
17 wide.

18 I do think that it is an extremely
19 responsible thing to do to undertake what is
20 in process, which is to identify, capture the
21 views as they've been expressed, because at
22 some point with passage of time, other things

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1 will happen and it will be visited in some
2 fashion or another.

3 And for that reason alone, I think,
4 having expended nearly a year's effort in the
5 work of the Subcommittee, that it's a valuable
6 contribution to at least capture what had been
7 expressed as this very wide group of divergent
8 views and it is far more complex than anything
9 that I had thought about coming in here.

10 There are aspects to this that are
11 fact-intensive, are complicated, and do have
12 impact upon other market participants, not
13 just the auditing profession.

14 So, I appreciate your efforts, Bob.

15 MEMBER GLAUBER: Well, Mr.
16 Chairman, I will again state the
17 Subcommittee's commitment to try and
18 accomplish just what you've asked us.

19 I think what we're seeking to
20 provide is a statement which reflects the
21 diversity of views in a balanced way, that it
22 doesn't favor one view over another. And it's

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1 in that spirit that I think we will work
2 forward to try and produce the paper you want.

3 CO-CHAIR NICOLAISEN: Good. Damon.

4 MEMBER SILVERS: Yes. Thank you,
5 Don. And I apologize for being late.

6 I have a couple of comments about
7 this Committee's work. First, on occasion
8 during the last few months, I've been involved
9 in the litigation discussion, and I would add
10 my compliments to Bob for all of his efforts.

11 I also -- I think it's been clear
12 from the beginning of this Committee's work
13 that this issue and this Subcommittee had
14 great -- was both an extremely important,
15 serious issue and one that had a certain
16 amount of peril for the overall mission of our
17 Committee.

18 And I think that Bob and the
19 comments of his Committee Members show a
20 commitment to not -- to working through a
21 difficult set of circumstances in a way that
22 allows us as a whole to move forward in our

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1 work, and -- express my appreciation for that.

2 Two more specific comments. First
3 -- and this goes, I think, to the spirit of
4 what I just said. I think that it's important
5 that, as the Subcommittee brings its final
6 language together as hopefully -- hopefully
7 doing what Tim laid out to do, it's important
8 that we not -- we not allow this matter to
9 become a matter that then gets sort of fought
10 line by line through the whole document, and
11 the sort of -- second- and third-order of
12 considerations take over.

13 I think that is the route to not -
14 - that is the route to sort of unraveling our
15 work and I'm very much opposed to doing that.

16 I know, I mean, I think we've successfully
17 avoided doing that so far.

18 Secondly, and off the litigation
19 subject, I believe that I understood, since I
20 came in late, I believe I understood Gaylen to
21 be referring in his comments a few moments ago
22 to the question of the fraud center and where

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1 that might be located, and I understand there
2 was some conversation about that before I
3 arrived.

4 I think it is important in setting
5 up such an undertaking that it be clearly
6 located in a public -- it has to have a sort
7 of public sector origin or route to it.

8 I think that, obviously, the
9 talents and -- the talents and resources of
10 the auditing profession and in its
11 manifestation in the firms, of academics and
12 of others, need to be brought to bear, but I
13 think it's extremely important that it be
14 under the umbrella or be shepherded in some
15 fashion by a body that is -- whose mission is
16 a public mission.

17 There are a number of different
18 possible sources of that. Gaylen does raise
19 one that I hadn't thought of, but I wanted to
20 make sure that that thought is, you know,
21 embodied in the record here, here today.

22 So, thank you.

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1 CO-CHAIR NICOLAISEN: Thank you,
2 Damon.

3 Barry.

4 MEMBER MELANCON: Thank you, Don.
5 I know that the Subcommittee worked real hard
6 on this -- on a lot of issues here and I think
7 -- you know, I could -- I won't repeat, but I
8 would support both Bill and Tim's comments.

9 I think the global issues of -- and
10 I'm sure they'll be captured in this fair and
11 balanced document that you're talking about,
12 Bob. I think that the --

13 MEMBER GLAUBER: In a fair and
14 balanced way.

15 MEMBER MELANCON: Right. I think
16 the US -- because, again, sort of my comments
17 like I said in the human capital area when we
18 were talking about the female representation
19 issue, the liability system in the US is -- is
20 a part of the US competitiveness or lack of
21 competitiveness issues that have to be
22 addressed in some form or fashion.

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1 And as you have global markets,
2 there are clearly different outcomes from a
3 liability perspective that exist as we could
4 use other examples, regulatory approaches, et
5 cetera, that have been discussed in other
6 approaches.

7 And so, I think getting those
8 points out there is a very important aspect.
9 I would ask that -- two things. One is on the
10 Recommendations related to, I guess,
11 transparency, and maybe it's at least one
12 other place in the document, there is a
13 reference to a size cut that is based on the
14 number of audits that a firm conducts. In
15 this case a hundred.

16 And I would strongly urge that that
17 is the wrong cut. And I understand where that
18 comes from because it's in the Sarbanes-Oxley
19 Act, and that's where PCAOB makes the line of
20 demarcation between an annual inspection and a
21 once-every-three-year inspection.

22 And I respect that. But, as we

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1 look at the mission of this, one of the things
2 that we focused on, and Damon's Committee has
3 focused on, is the issue of more options in
4 the marketplace, the competitiveness of other
5 firms, et cetera.

6 And I know, in dealing with these
7 firms, which below the top six or seven firms,
8 eight firms, I deal with a tremendous amount.
9 And the issue of what these requirements are,
10 whatever the Recommendations are, being a
11 decision point to them as to whether they go
12 over the number of audits, the hundred audits.

13 And I don't think we want a
14 Recommendation that builds into a smaller
15 firm's psyche and decision-making process that
16 I'm going to do, you know, 95 audits and not
17 go up again.

18 I think we need to apply a risk
19 approach to this. And the way I think the
20 risk approach is, would be on the size of
21 audits.

22 So, you know, if -- I would argue -

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1 - I'm not saying this is the only way to do
2 it, but, you know, something that would say,
3 these Recommendations would apply to a firm if
4 you've audited a Fortune 500 at any time in
5 the last three years, as an example, because
6 that goes to the investor risk, the capital --
7 the larger capital environments as well.

8 And it doesn't put into the system
9 a disincentive for firms to continue to grow
10 to be other viable options in the marketplace
11 in a certain size spectrum.

12 So, I would strongly urge a change
13 in that wording, regardless of what the
14 ultimate Recommendation is, but the
15 applicability to it.

16 And then the last point is on the
17 transparency issues, and there is some wording
18 to this. I would -- you know, to the extent
19 you are editing this or whatever, I think the
20 tie of -- to quality, quality indicators, I
21 think, Zoe-Vonna talked about that at a couple
22 of the last meetings, et cetera, is the real

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1 investor protection point.

2 And I think the profession is -- is
3 very receptive to those types of things. And
4 so I would -- I would continue to reemphasize
5 that as you work and get to the final
6 recommendations in those areas.

7 But that first point on the size
8 continuum, I wouldn't want to undo some of the
9 -- some of the notions to the smaller firms
10 that we have.

11 CO-CHAIR NICOLAISEN: Right. And
12 I'm certain that all of the Subcommittee
13 Chairs would be happy to entertain a -- you
14 know, any edits or any suggestions that you'd
15 care to forward to them, and it may be an
16 efficient way to do it as well.

17 Gaylen.

18 MEMBER HANSEN: Yes. I was just
19 going to follow up with Barry's comments. I
20 think what he's describing here is an accurate
21 description of what's taking place in the
22 marketplace.

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1 Firms will -- not necessarily not
2 want to -- what will happen is they'll cull
3 out their client lists and drop the smaller
4 ones at the very bottom of the 100 list so
5 that they don't go over 100.

6 And I would happen to agree with
7 you that that's not the outcome that we want
8 in terms of sizing. So, I think that that's
9 something that we should, you know, perhaps
10 consider.

11 CO-CHAIR NICOLAISEN: Damon.

12 MEMBER SILVERS: We've now had
13 several comments about our work in the context
14 of a global -- globalizing capital markets,
15 and I think it's important that, as we're
16 having a public meeting, that something be
17 said about the way that at least some
18 investors think about this matter.

19 Because, I think they're -- as Don
20 observed about litigation, it's more complex
21 than it seems. The United States has --
22 continues to have, I think, a pretty widely-

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1 accepted premium on company cash flows.

2 If you list in our markets you will
3 get a better multiple than if you get in other
4 markets. This is extremely important to
5 maintain in the context of the United States'
6 current account deficit and our dependence on
7 foreign capital flows to finance the current
8 way in which we manage or mismanage our
9 economy.

10 And it is difficult to unpack all
11 the factors in the way we do things that
12 produces that extra multiple. The -- and it
13 is dangerous, both to investors and to the
14 country to start dismantling those, sort of
15 piecemeal, aspects of our system, our capital
16 market system that gives comfort to investors
17 that their money is safe, and that the
18 information they're investing based on is
19 relatively accurate.

20 That being said, there definitely
21 is a trend toward a single global capital
22 market. And there is -- it will be, in the

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1 long run, irresponsible of the major actors in
2 the world economy not to construct a unified
3 oversight system for that unified market.

4 In fact, it's clearly obviously
5 irresponsible now that we have no such thing.
6 And, if you look at the differences in the way
7 in which markets are regulated -- the major
8 markets are regulated, the United Kingdom,
9 continental Europe, Hong Kong, et cetera,
10 there are many differences in many areas, and
11 some of those differences the business
12 community or the audit firms prefer the US
13 version, and some, they prefer the overseas
14 version or versions, and investors, likewise.

15 The need for a process to begin to
16 create frameworks, to have a single system is
17 dire, but it would be extremely dumb to start
18 acting unilaterally before such a framework
19 discussion is in motion, because of the things
20 I alluded to earlier.

21 And I am hopeful that that
22 framework discussion is in the process of

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1 coalescing slowly in a variety of different
2 ways.

3 I can point people to, in areas
4 outside of the auditing profession, to
5 extensive conversations between leaders in the
6 European Parliament and leaders in our
7 Congress about the -- what the term is, the
8 shadow banking system, about private pools of
9 capital.

10 Clearly, there's a whole discussion
11 that some people in this building have taken
12 part in in relationship to the credit crisis
13 with their European and global counterparts.

14 There are obviously many
15 discussions that investors take part in in
16 relationship to trying to see aspects of non-
17 US regulatory systems that we like
18 incorporated in the US system, ranging from
19 the kinds of transparency issues around audit
20 firms that we have had in front of us to a
21 variety of corporate governance devices that
22 exist, particularly in the UK that investors

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1 like.

2 This complex fabric -- and this
3 extremely politically-complicated and kind of
4 long-term process is one that is, I think,
5 recognized by everybody who's familiar with
6 the way that the markets are moving. It's
7 just a vital, vital process.

8 But, you know, the one thing that
9 you don't do, I think -- I think we all know,
10 the one thing that you don't do is when you're
11 going to enter into such a kind of complex
12 negotiation, you don't make all your
13 concessions before you reach the table.

14 And I think that's, in a nutshell,
15 the way investors look at this. I also think
16 that the question of what is good for the
17 United -- for US competitiveness in relation
18 to this set of issues, I think has often
19 gotten completely backwards, that what is good
20 for US competitiveness in this area is what
21 will maintain that -- that excess multiple.

22 And having integrity in our markets

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1 represented by effective auditors with a clear
2 sense of professionalism and a clear sense of
3 accountability has got to be a pillar of that.

4 And so, in fact, weakening those
5 structures is not just not pro-competitive, it
6 is harmful to the competitiveness in our
7 markets in the ways that matter most, both to
8 investors in the markets as a whole and our
9 nation, so long as we continue to need these
10 foreign capital inflows in the way we do
11 today.

12 CO-CHAIR NICOLAISEN: Great. Thank
13 you.

14 Bob.

15 MR. HERZ: I apologize if this was
16 already covered when I stepped out to comb my
17 hair.

18 In regard to Recommendation 6 and
19 the Recommendation that the certain audit
20 firms, you know, whether it's 100 or how you
21 do the cut, file audited financials
22 confidentially with the PCAOB.

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1 I just wanted to, both for my own
2 benefit, but maybe also the report might
3 benefit from kind of the Committee's thinking,
4 Subcommittee, and the Committee's thinking on
5 that because we heard, I think, fairly strong
6 testimony both ways on the issue.

7 Some private, primarily, investors
8 saying we think that they ought to file --
9 make generally available audited GAAP
10 financials and pointing to the UK model and
11 the like, and then others countering, but
12 we're not the UK. We have our litigation
13 worries, and why is that necessary for
14 understanding -- you know, how does that
15 contribute to the objectives that we're trying
16 to attain?

17 And so, I'm not going to make a
18 judgment in balancing those two things, but
19 you came to this conclusion that somewhere in
20 between those two ideas to ask, starting in
21 2011, I think, for these firms to, with the
22 PCAOB file audited GAAP, or maybe by that time

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1 IFRS or whatever, financial statements.

2 And I'm just kind of interested,
3 because I don't think when I read the report,
4 which is very succinct, I kind of understood
5 exactly how you came to that, other than that
6 it's somewhere in between and why you think
7 that might still be of benefit for -- you
8 know, the reasons behind that.

9 MEMBER GLAUBER: Well, let me at
10 least start to respond for the Committee,
11 Subcommittee. I think the additional color
12 you've given has been quite proper. There was
13 a diversity of positions, as you have
14 summarized as to whether these should be made
15 public or not.

16 And this represents the
17 Subcommittee's consensus position among those
18 different positions. One can make arguments
19 on both sides, as you did in your summary, and
20 I think this is the position the Subcommittee
21 has come to, knowing that it should support
22 this and the entire Committee should support

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1 this by consensus.

2 MR. HERZ: I guess, and I kind of
3 say, okay, I'm Mark Olson now in 2011, and I
4 start getting these and, okay, they're in some
5 confidential file and I benefit from your
6 insights as a former regulator, you know,
7 what's Mark supposed to do with these, and
8 it's not clear to me.

9 MEMBER GLAUBER: Well, he can do
10 with them as he chooses. This Subcommittee is
11 not going to tell him, is all. I could
12 imagine sustaining a number of positions.
13 And, in fact, the world, by 2011 may be very
14 different as regards the public availability
15 of these audited financial statements.

16 I don't know, but -- and it may be
17 very different, by the way, with regard to
18 issues that Damon spoke so eloquently about,
19 the litigation issues.

20 But, in that context, I would
21 imagine that the then head of the PCAOB will
22 make some determination within the guidance

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1 that the PCAOB receives.

2 CO-CHAIR NICOLAISEN: I'll add just
3 a little more color to that. Chairman Levitt
4 and I also sat in on these discussions and I
5 think we're satisfied that the Committee had
6 really done its work, had taken conclusions
7 where they had a major consensus, that there
8 was adequate give-and-take, that it was a very
9 good process and that we were -- we were in
10 our place with the progress that would be made
11 by implementing this recommendation.

12 Neither Chairman Levitt, nor I
13 think that this should be the end of it. Our
14 strong views for a lot of reasons, most of
15 which lead to, or revert back to transparency
16 and public interest, are that the firms should
17 have their financial statements available to
18 the investing public.

19 And I think we will be very clear
20 on that as we express our views in the final
21 report. But for purposes of the
22 Subcommittee's work, and I'd have to say that

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1 it represents tremendous progress and a lot of
2 give and a lot of take, and we're willing to
3 readily accept that and are appreciative of
4 the work that the Subcommittee has done.

5 I think it's an important
6 milestone.

7 MR. HERZ: Thank you. I think that
8 helps me -- helps me a bit, sort of -- I mean,
9 you know, I would also agree that just the
10 exercise of going -- preparing audited
11 financials to be audited is a good exercise
12 and obviously, in itself.

13 That's kind of the premise we're
14 working on generally on this Committee, but it
15 wasn't clear to me whether, you know, as Bob
16 said, he doesn't know what they would do,
17 whether there's some kind of a procedure, the
18 capital adequacy, something else that the --
19 that would be expected and the public would
20 say, Okay. What? That's nice.

21 CO-CHAIR NICOLAISEN: Great. Thank
22 you.

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1 Anyone else? Alan.

2 MEMBER BELLER: Revisiting
3 globalization yet one more time, I share the
4 view and I share almost all the views that
5 Damon expressed with respect to globalization.
6 I think protecting our market premium is
7 critical.

8 I think that there are other
9 elements of competitiveness of the capital
10 markets that are also critical, although I
11 certainly, not for an instant, believe that we
12 should sacrifice investors to any of them.

13 Where I do worry is I think waiting
14 for successful development of global capital
15 markets regulation, which is the right
16 ultimate objective, it's something I've been
17 waiting for and a little bit of working for
18 towards since about the early Eighties.

19 I think its realization is somewhat
20 like the realization of world government,
21 however, which is that it's going to take a
22 while. And the markets will not stand still

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1 and wait for it.

2 And what that means is that all of
3 our market participants, including investors
4 and all of our regulators and self-regulators
5 have to operate with a keen realization of the
6 directions in which the market is going,
7 absent probably some of the neat structures
8 that we'd like to have.

9 And I think that -- whatever the
10 outcome of our debate about litigation reform
11 and countless other things, what that means is
12 that our regulators and market participants
13 have to operate to the extent they can
14 effectively, multilaterally in a global
15 environment.

16 That means working very hard to
17 make sure that US regulators have a seat at
18 the various global tables, that other US
19 market participants have an effective voice
20 and an effective seat at various global
21 tables.

22 I think what, you know, what the

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1 FASB or the IASB have been doing since 2000 is
2 an example of how that can work.

3 That's going to be the task that we
4 face, and while I certainly agree with Damon
5 that unilateral action without an appropriate
6 regard for what can be done multilaterally and
7 what can be -- and what has to be done in our
8 interest is not a good way to go.

9 I would also note that there's a
10 corollary to that, and I'm quite confident
11 it's a corollary that Damon agrees to as well,
12 though I won't put words in his mouth, and
13 that is that unilateral failure to take action
14 in those same circumstances, leaves you --
15 could leave you in the same place.

16 And so I think it's -- it's not a -
17 - we can sit on our hands and wait to see what
18 happens. We have to be thoughtful. We have
19 to engage. And that is the right way to deal
20 with globalization.

21 CO-CHAIR NICOLAISEN: Alan, thank
22 you.

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1 And, Damon, thank you.

2 I think that this is an important
3 area that is touched on in probably every
4 aspect of the Recommendations that we have,
5 whether directly or indirectly; we are part of
6 a global society, and we need to be aware of
7 that, and I think Alan's view, I share, that
8 we -- it will be better if we're part of the
9 solution than if we're not engaged.

10 So, I support, and I think Damon,
11 you're in exactly that same place, and we
12 support that. And I don't want to -- as much
13 as I love this topic, I don't want to occupy
14 the rest of the afternoon on globalization,
15 but I thank you for that input.

16 Bob, anything else from your
17 Subcommittee?

18 MEMBER GLAUBER: Well, I had
19 intended to give a 15- or 20-minute talk on
20 the issue of globalization, but I think I've
21 just been told you prefer that not.

22 We can engage this issue and it

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1 will be, I'm sure, in the final report. It is
2 an issue that we cannot avoid, as we've all
3 said, so let me just leave it there.

4 CO-CHAIR NICOLAISEN: Great. Well,
5 than you very much. Thanks, Bob, for your
6 leadership on this Subcommittee. Thank you
7 very much to all the Subcommittee members.

8 While the debate has been lively
9 and spirited within the Subcommittee, as
10 you've also seen here, I've been particularly
11 impressed by the respect that everyone has
12 shown for the points of views that have been
13 raised with which they may not readily agree.
14 And I think that's a test of how successful
15 this process has been. So, I thank you for
16 that.

17 Let's move on to Damon Silvers and
18 your Subcommittee on Concentration and
19 Competitiveness.

20 MEMBER SILVERS: Thank you, Don.

21 We have made a series of
22 meaningful, but not structural changes, I

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1 would say, to the draft in our area. I will
2 go through them briefly. In the order which -
3 - not in the order of their importance
4 necessarily, but in the order in which they
5 appear in the document.

6 The first is, we had in -- both in
7 the comments we received and the deliberations
8 of our Subcommittee a great deal of interest
9 in barriers that exist, and I think the belief
10 of the Subcommittee is that some of them are
11 inappropriate.

12 Barriers that exist to firms
13 changing their auditors, and a concern based,
14 I think, on the members of our Committee's
15 experience with these particular moments in
16 the life of a business that the departing
17 auditor is not always appropriately
18 collaborative in relation to that.

19 And so there's new language on page
20 -- in Recommendation 1. I'm not going to give
21 you the page number. Recommendation 1, that
22 notes there are significant costs associated

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1 with changing auditors and fees can be charged
2 for predecessor auditor's opinion on
3 previously filed financial statements, and
4 urges auditors that predecessor auditors fully
5 cooperate and communicate with their successor
6 auditors, and we've had some discussions about
7 how one might, from a sort of oversight
8 perspective, encourage that.

9 This is -- Members of the
10 Subcommittee have been particularly active in
11 considering and framing these recommendations,
12 and I invite Ken and Mary to chime in here
13 when I'm finished and make sure I get these
14 concerns properly captured.

15 Secondly, we have a Recommendation
16 1(a) that mandates -- that recommends the
17 disclosure of agreement provisions that
18 issuers enter into, limiting their choice of
19 auditor.

20 In the initial language in this
21 area we had talked about that disclosure in
22 the context of a registration statement.

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1 We've now broadened that to include 10K and
2 proxies, you know, to capture ongoing
3 businesses that enter into such agreements.

4 In Recommendation 1(b), where we
5 had urged that regulatory bodies, the
6 government agencies, make efforts to
7 incorporate smaller firms in the variety of
8 places where they involve and consult with the
9 auditing profession.

10 We now note those programs that do
11 exist now that do do -- that are focused on
12 that. The SEC's Office of Small Business
13 Policy, the PCAOB's Forum on Auditing in the
14 Small Business Environment and FASB's Small
15 Business Advisory Committee.

16 I think we do so, I am not going to
17 read you the language, but we do so with a
18 certain amount of compliment to all involved.

19 Fourth, in Recommendation 2(b)
20 which is the rehabilitation mechanism, it has
21 been the Committee's view, I think, really
22 from the beginning, that this mechanism does

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1 not work in the context in which there's an
2 issue as to whether an audit firm would have
3 committed a crime where there is a question
4 about that or there's a question about whether
5 a firm's leadership is moving in the direction
6 where, if they haven't committed a crime, they
7 might soon, that this mechanism isn't going to
8 work if there isn't some communication between
9 the SEC, which would have the triggering
10 authority under the rehabilitation mechanism,
11 and the criminal authorities, the Justice
12 Department in particular.

13 This is a very -- this is very
14 touchy business because it is at least not my
15 personal intention to in any way suggest that
16 there ought to be a double standard here in
17 our criminal law.

18 And the -- or that in any way the
19 Committee was seeking to limit or muzzle the
20 Justice Department in its carrying out of its
21 duties.

22 So, this required a certain amount

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1 of interaction with the Justice Department.
2 The Justice Department are busy people and
3 it's taking a little time to get us there.

4 And we do have language now that
5 lays out the notion that there ought to be a
6 -- that the Justice Department ought to be in
7 touch with the SEC when this sort of matter
8 arises with respect to a -- with respect to a
9 firm that is covered by the rehabilitation
10 provision.

11 And the Committee is satisfied with
12 the language we have, the Justice Department
13 is satisfied with the language we have, and I
14 consider that no small achievement.

15 CO-CHAIR NICOLAISEN:
16 Congratulations on that.

17 MEMBER SILVERS: So, the next --
18 the next language, we have a Recommendation 3
19 that goes to the disclosure of audit quality
20 indicators by audit firms and the PCAOB
21 working on trying to define what appropriate
22 indicators would be.

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1 Here, there was some discussion of
2 the notion that there ought to be both
3 indicators that are output-based and input-
4 based. Output-based means results in terms of
5 -- and there could be many different ways of
6 measuring the results from audit firms.

7 Input-based would mean things like
8 partner, personnel per client or that sort of
9 stuff. I mean, the resources put into
10 auditing by the firm or resources put into
11 human capital development by the firm, a
12 variety of indicators about the strength of
13 the firm not going to what its actual audit
14 results are.

15 So, that distinction and the
16 Committee's interest in seeing both types of
17 indicators explored, is now made clear in the
18 document.

19 Recommendation 5 notes that -- that
20 there might be an interest on the part of
21 audit committees and investors in obtaining
22 data beyond the name of the senior audit

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1 partner, engagement-specific data, such as the
2 auditor's tenure with the public company, that
3 should be disclosed in conjunction with the
4 shareholder vote on selection of auditors.

5 Finally, and this was the subject
6 of some discussion at our last open meeting,
7 based on a question from Gaylen Hansen. The
8 Subcommittee solicited the views of smaller
9 audit firms on the impact of globalization.

10 I don't mean to start that again,
11 but we did -- we did follow up on Gaylen's
12 comments and solicit those views, and we
13 received several very thoughtful comments from
14 the smaller firms, for which we are grateful.

15 The gist of those comments, I
16 think, really was that globalization does
17 represent both some significant challenges to
18 those firms, and there was some -- some
19 listing of what those challenges were.

20 The firms did not go into much
21 greater detail than that, or become -- or go
22 from the listing of the challenges to being

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1 prescriptive about how those challenges might
2 be approached by this Committee or by other
3 people involved -- other institutions involved
4 in the structuring of the global auditing
5 environment and the accounting environment.

6 The Committee felt that in this
7 circumstance, that the appropriate approach
8 that was then to add language to this final
9 section, noting just that, that there were --
10 that there were challenges that the auditors,
11 smaller firms felt that they faced in a
12 globalizing environment and make a few
13 references to what some of those challenges
14 were.

15 And note that it was the
16 Committee's view that regulators, those
17 involved in structuring that environment be
18 attentive to those challenges and seek to
19 mitigate them as much as possible in the
20 interest of the overall purposes of our
21 recommendation in terms of strengthening
22 smaller firms and enhancing broader -- a

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1 broader degree of competition in the market
2 for public company auditing services.

3 I believe that concludes the
4 changes we've made. I'll ask my fellow
5 Committee Members if I've missed anything or
6 mischaracterized anything or if there's
7 anything they'd like to add on any of the
8 items.

9 MEMBER GOLDMAN: Thanks. No, I
10 would actually -- I'm not going to add too
11 much. I actually wanted to do a thank you.
12 It's amazing to me sometimes how some words we
13 sort of put mumbo-jumbo, and all of a sudden
14 they come back from the Treasury Staff and
15 they are so lucid.

16 So, I do want to express my total
17 thanks to a very well -- in my opinion,
18 anyway, a very well-written document and there
19 really is a lot of thanks to the Treasury
20 Staff. So, that's really my first point.

21 The second point is, I think the
22 thing we always -- we strive to do, and I'm

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1 happy with it, is to create directionally
2 substantive, actionable recommendations so
3 that -- so something will come out of this and
4 be important going forward.

5 And I feel, as Damon has said, that
6 we do -- we have developed a set of
7 recommendations that will provide -- will be
8 very helpful in this process. That's -- even
9 though some of them have been controversial.

10 Also, thanks to Alan Beller for
11 Recommendation 2, because he was really very
12 instrumental in sort of the -- that's one of
13 the "Ah has!?" in life, when you go through a
14 committee and you are looking for really a key
15 recommendation and he was very helpful in
16 crafting that.

17 The last point I would say is this
18 was one that Damon mentioned relative to -- to
19 me it's really important with -- and some of
20 the data does definitely suggest we are going
21 in the right direction in terms of more
22 competitiveness amongst the various auditing

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1 firms, and so that was sort of the basis of
2 one of my thoughts here relative to continuing
3 to improve the competitive environment which
4 means the ability to relook at other auditing
5 firms, other than the one you're currently
6 utilizing.

7 So, I just know as a -- from my
8 perspective, both as a CFO, as well from many
9 boards, there definitely tends to be
10 reluctance to engage -- you know, to gauge, in
11 putting out for competitive bid, if you will,
12 to look at other firms.

13 It comes from really several
14 vantage points. One is, you are concerned
15 about the costs from the outgoing firm.
16 You're concerned about the opinions that they
17 may come up with, your concern about the
18 various work papers, whatever, that they may -
19 - you may need to have transferred.

20 Also, it's interesting, you are
21 concerned about the way a different firm or
22 even a different partner may look at the same

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1 facts and come out to a different conclusion.

2 It turns out that also occurs in
3 the same firm many times. And so, one of the
4 risks you always have when the five-year
5 rotation, is a new partner may see the facts
6 in a different light, and you end up going
7 through, and actually, in some cases, changing
8 some of the judgments you've made previously.

9 But the gist of what we've tried to
10 add here is to -- again, I'm not sure it's
11 perfect yet, but at least the gist is to
12 create a more level playing field -- maybe
13 that's what I want to say -- a more level
14 playing field so that firms can more easily
15 from time to time put out for bid, if you
16 will, and look at other auditing firms and
17 make a selection on a whole variety of
18 different criteria, some of which, by the way,
19 may come out -- come up with some of the audit
20 quality metrics we asked for.

21 It may come up with some of the
22 financial statements we've asked for, although

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1 right now they're still very private, so that
2 is some of the basis that I think, as we go
3 from four large to maybe six or eight or a
4 hundred, however you want to look at it, is
5 the more you have a level playing field to
6 compete, I think will be very helpful for this
7 industry.

8 MEMBER SILVERS: Don, could I just
9 add one more thing I neglected to say, which
10 Ken reminded me of.

11 You go first.

12 MEMBER BUSH: No, no.

13 MEMBER SILVERS: All right. Very
14 briefly, that although it's not our
15 Committee's work, that the Committee -- our
16 Subcommittee took an intense interest in the
17 transparency issues that the Firm Structure
18 Committee was taking up.

19 Our Committee is made up largely of
20 investors and people involved in the audit
21 committee processes, and very much wanted to
22 see increased transparency.

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1 I think that -- I'm not sure that
2 we're really satisfied with it being held in a
3 vault some place at the PCAOB, but we're also
4 really interested in the consensus and moving
5 forward.

6 But I thought it was important to
7 register, you know, the strong feelings, I
8 think, on the part of our Committee, that this
9 was an important initiative that Bob has
10 shepherded through to consensus.

11 CO-CHAIR NICOLAISEN: Great. Thank
12 you.

13 Mary.

14 MEMBER BUSH: Thank you. First I
15 want to just echo Ken's comments about
16 compliments to the Treasury Staff for making
17 good, lucid material out of our mumblings.
18 They were outstanding.

19 I also want to compliment Damon for
20 really being an outstanding Chairman and
21 pushing our work -- our work forward, with
22 high quality.

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1 The general comment that I would
2 like to make really reflects back on some of
3 the comments that were made earlier about
4 globalization and what's happening in the
5 global capital markets.

6 You know, as I look at, you know,
7 particularly our Subcommittee's work, but then
8 really the work of the entire Committee, it's
9 really all about not sitting still while
10 global markets are changing, and maintaining
11 the edge for our markets, but also not sitting
12 still as we face the extraordinary challenges
13 in the capital markets that we are facing
14 today.

15 And, as I think about our
16 Subcommittee's work, you know, I think it
17 moves from the end of prevention all the way
18 to the end of a process when something --
19 something catastrophic happens.

20 And in the category of prevention,
21 some of the things that Damon has mentioned,
22 you know, the development of indicators by the

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1 PCAOB of audit quality, the monitoring of
2 those indicators if the PCAOB so agrees to do
3 that.

4 And all of that, of course, goes to
5 the issue of transparency and hopefully to the
6 issue of prevention, in case there are
7 problems, you know, with a -- with one of the
8 auditing firms.

9 And then at the other extreme, of
10 course, is the mechanism that Damon referred
11 to that Alan helped us develop which I think
12 is extremely important.

13 And the one thing that I want to
14 point out about that that I thought was really
15 essential for that mechanism to make sense in
16 a well-rounded way, is the inclusion of the --
17 if you will, the opinion or the satisfaction
18 of the Justice Department with the language,
19 because I think the key point there is not so
20 much their notifying the SEC if they are about
21 to bring criminal investigation.

22 The key point is really that the

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1 discussions are held early and that they
2 understand the consequences of any action that
3 they might -- that they might be contemplating
4 taking.

5 So, I think that's just hugely
6 important and I think it's a major step
7 forward so that hopefully we would not
8 experience the kind of situation where another
9 major auditing firm was taken out, if you
10 will. Thank you.

11 CO-CHAIR NICOLAISEN: All right.
12 Thank you.

13 Tim Flynn.

14 MEMBER FLYNN: Just a couple words
15 on the work. I think it's very good work that
16 you all have done. I think one only has to be
17 in the profession to feel the competitiveness
18 of it. It is a very competitive profession
19 and I think with all this discussion, we
20 shouldn't lose sight of that.

21 You compete for business every day
22 on quality, in talent, and it's very, very

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1 competitive.

2 I would ask the Subcommittee to go
3 back and look at the language that came in
4 around auditor change and access to work
5 papers and those types of things.

6 It clearly doesn't reflect my view
7 in a broad sense, in particular with some of
8 the discussion about high fees being charged
9 and so forth.

10 I'd like to get a sense for the
11 testimony or just some of the background
12 around that because that, to me, is not -- is
13 not how the profession behaves, and I think
14 the profession works very strong to
15 communicate when all of the transitions do
16 happen, once that's been decided, and work
17 through very difficult issues sometimes
18 because sometimes with changes you revolve
19 around regulatory environments or litigation
20 issues.

21 And so I think you have -- I'd like
22 to make sure that you just go back and look at

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1 that in context. I know there's a footnote
2 representing an anonymous private investor,
3 former auditor and former CFO on that section,
4 and I guess I would just ask him a point of
5 process.

6 If someone doesn't come forth with
7 their name and says they're anonymous, I'm not
8 sure we should credit too much in footnotes to
9 anonymous letters. That might be something we
10 should think about in terms of how we're going
11 to put substance and what gets access into the
12 report.

13 So, those are just some comments
14 that I'd like to make in regards to the work,
15 but overall, I really appreciate the effort
16 you've put forth.

17 CO-CHAIR NICOLAISEN: Good. Thank
18 you, Tim.

19 Rick.

20 MEMBER MURRAY: Thank you, Don.

21 Throughout this Committee's life
22 Damon has been both clear and articulate in

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1 expressing his view, and I assume, of others
2 on his Subcommittee, that litigation is deemed
3 a valuable motivator to audit quality and an
4 strength of the competitiveness of the US
5 marketplace.

6 That is, of course, one of the key
7 issues on which the Structure and Finance
8 Subcommittee has wrestled throughout that
9 year, having been assigned responsibility for
10 dealing with that topic and one of the issues
11 on which we have come to a clear and
12 articulate impasse.

13 Damon asked in his opening remarks
14 earlier that we not try to tinker with the
15 language elsewhere in the report, and I accept
16 the challenge insofar as I'm able.

17 There are two issues, Damon, that I
18 would ask be given further consideration on
19 the proposition that language, as it exists
20 currently in your report, ignores the impasse
21 that the Subcommittee with the primary
22 responsibility for this has come to.

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1 One of those is on, in the opening
2 paragraph of your Recommendation 2 you note
3 the problem of the issue of catastrophic risks
4 and follow it with the statement, these risks
5 include general financial risks and risks
6 relating to failure in the provision of audit
7 services and non-audit services, including
8 civil litigation.

9 In my view, that attempt to be
10 balanced is perhaps not entirely successful,
11 and leaves an undue impression that audit
12 failure is the greater cause of this problem.

13 And I would ask that you and your
14 Committee consider whether, because this is
15 merely descriptive and not operational, you
16 might accommodate our impasse in a manner
17 that's a bit more -- or even reference our
18 impasse when it is articulated. It may be a
19 way to deal with this.

20 The second issue that I was not
21 able to pass by deals with your recommendation
22 to second-step -- and that's on page 13 in

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1 this presentation.

2 In describing the effect of
3 adopting this recommendation, you use the
4 language, in order to ensure the stable
5 functioning of the capital markets.

6 I read that as a very strong
7 statement of confidence that this
8 Recommendation 2 will be a solution to the
9 concern about the elephant that Gary Previts
10 describes, and will put to rest any need to
11 worry about the business model and
12 sustainability of the large firms.

13 I don't question your right to make
14 the recommendation, but I would ask here again
15 if you might acknowledge that this is an
16 aspiration and not an expectation.

17 MEMBER SILVERS: Can I ask where
18 that sentence is?

19 MEMBER MURRAY: Page 13. It is the
20 second paragraph under second step, the third
21 line --

22 MEMBER SILVERS: Oh, yes, I see.

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1 Okay.

2 MEMBER MURRAY: I would have said
3 nothing more, Damon, if you hadn't made your
4 observation about your distress over our
5 transparency conclusion.

6 I would suggest that I have a
7 similar discomfort with your recommendation,
8 that there be shareholder approval annually
9 for the appointment of auditors, but in a
10 similar spirit of good will, I would accede to
11 your right to make that recommendation.

12 MEMBER SILVERS: May I respond for
13 a moment?

14 CO-CHAIR NICOLAISEN: Absolutely.

15 MEMBER SILVERS: It's certainly not
16 the intention of the Committee, in looking at
17 this language, to suggest an agreement about
18 some of the sort of ultimate concerns that
19 Rick was discussing where there is none.

20 And it strikes me that, Rick, your
21 comments on this particular language you are
22 pointing to in you concern should be easily

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1 resolvable. I don't think we need to
2 negotiate it here today, but I think we can
3 work that out to your satisfaction.

4 MEMBER MURRAY: Thank you very
5 much, and just a final comment. I heartily
6 endorse everything that Bill Travis said about
7 the sad consequence of our being unable to
8 agree, and Bill, I appreciate your putting
9 that view forward.

10 I share your view. I don't share
11 your confidence that we have the capacity to
12 improve upon where we are.

13 CO-CHAIR NICOLAISEN: Thank you.
14 Any of our Committee members that have joined
15 by telephone, any questions, comments,
16 suggestions?

17 CO-CHAIR LEVITT: Keep the faith.

18 CO-CHAIR NICOLAISEN: I'm sorry?

19 CO-CHAIR LEVITT: Don, this is
20 Arthur.

21 CO-CHAIR NICOLAISEN: Oh, Arthur.
22 Good afternoon to you. Anything that you'd

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1 like to add to this or ask about?

2 CO-CHAIR LEVITT: Well, you know, I
3 think that we have a difficult undertaking,
4 but I think the fact that we've approached it
5 with the kind of openness and civility leads
6 me to believe that we're going to come out of
7 this with some significant Recommendations and
8 in those areas where we have not been able to
9 arrive at consensus, I think we'll be able to
10 define the areas of contrast in a way which I
11 think will also be constructive.

12 And I think the Committee Chairs
13 have done an absolutely fantastic job.

14 CO-CHAIR NICOLAISEN: Great. Thank
15 you very much.

16 I don't want to cut this off if
17 there are others who would care to add
18 anything to this discussion.

19 (No response.)

20 CO-CHAIR NICOLAISEN: Hearing none
21 and seeing no tents going up, we are now at
22 that point where the -- the body of the report

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1 that includes recommendations is pretty far
2 along.

3 Our next meeting is scheduled for
4 Friday, September 26th. We believe we're
5 going to be able to do that telephonically.
6 That's our plan.

7 In the interim period what we would
8 like to have happen today is to have this
9 Committee approve for posting in the public
10 record for a 30-day comment period, the draft
11 as it is now existing, recognizing that, of
12 course, we heard some things today, and there
13 will be some modifications as we continue to
14 work our way through the process.

15 I would entertain a motion to call
16 for that vote.

17 MEMBER PREVITS: So moved.

18 MEMBER GOLDMAN: Second.

19 CO-CHAIR NICOLAISEN: Thank you
20 very much. Thank you.

21 And we'll ask Treasury to do a roll
22 call of each individual member.

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1 MR. LAUGHTON: Mr. Beller.
2 MEMBER BELLER: Yes.
3 MR. LAUGHTON: Ms. Brinkley. Not
4 here.
5 Ms. Bush.
6 MEMBER BUSH: Yes.
7 MR. LAUGHTON: Mr. Cohen. Not
8 here.
9 Mr. Flynn?
10 MEMBER FLYNN: Yes.
11 MR. LAUGHTON: Mr. Glauber.
12 MEMBER GLAUBER: Yes.
13 MR. LAUGHTON: Mr. Goldman.
14 MEMBER GOLDMAN: Yes.
15 MR. LAUGHTON: Mr. Hansen.
16 MEMBER HANSEN: Yes.
17 MR. LAUGHTON: Mr. Levitt.
18 CO-CHAIR LEVITT: Yes.
19 MR. LAUGHTON: Mr. Melancon.
20 MEMBER MELANCON: Yes.
21 MR. LAUGHTON: Ms. Mulcahy. Not
22 here.

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Mr. Murray.

MEMBER MURRAY: Yes.

MR. LAUGHTON: Mr. Nicolaisen.

CO-CHAIR NICOLAISEN: Yes.

MR. LAUGHTON: Mr. Previts.

MEMBER PREVITS: Yes.

MR. LAUGHTON: Mr. Silvers.

MEMBER SILVERS: Yes.

MR. LAUGHTON: Mr. Simonson. Not

here.

Ms. Smith.

MS. SMITH: Yes.

MR. LAUGHTON: Mr. Travis.

MR. TRAVIS: Yes.

MR. LAUGHTON: Mr. Turner. Not

here.

Mr. Volcker.

MR. VOLCKER: Yes.

MR. LAUGHTON: Ms. Yerger.

MS. YERGER: Yes.

CO-CHAIR NICOLAISEN: Excellent.

Sounds like the ayes have it, and that we did,

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1 in fact, maintain more than our quorum. And I
2 thank everyone for that.

3 I want to especially thank Treasury
4 Staff. They've been working incredibly hard,
5 very, very long hours and I'm always shocked
6 to get emails and responses to phone calls on
7 Saturday nights and Sunday mornings and every
8 other time in between and I recognize that
9 that has taken it's toll. It's not an easy
10 thing to do, and I'm sure that all of us want
11 to express our appreciation to Treasury Staff
12 for doing that. We really sincerely do
13 appreciate your efforts, and we thank you.

14 (Applause.)

15 CO-CHAIR NICOLAISEN: I'd also note
16 that Zoe-Vonna Palmrose, I believe, is
17 returning back to the academic world, will be
18 leaving the SEC at the end of this month.

19 She has been a very, very important
20 contributor to our efforts as an observer, and
21 we would hope that you would continue, Zoe-
22 Vonna, to provide your input and support, and

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1 we wish you all the best as you return to the
2 academic world, and bring the messages that
3 you've heard this Subcommittee make would be
4 appreciated.

5 Our observers. Thank you. It's
6 tough to be the observer and not hold the pen,
7 and I know that for those of you who are in
8 that position, it's a real challenge, but we
9 thank you for your support.

10 We thank you for your questioning.

11 We thank you for your civility, and we look
12 forward to your continued input as we bring
13 this report to conclusion.

14 Those watching by webcast, those of
15 you in our audience, elsewhere, we would
16 certainly encourage you to continue to comment
17 during this 30-day comment period on the
18 report as it's crafted at this point in time.

19 I think you've heard that there
20 will be some thought about some of the
21 ultimate wording that will be in the document,
22 and there's a very important piece from Mr.

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1 Glauber's Subcommittee that continues to be
2 worked on.

3 All input is appreciated, and I
4 thank you for your time, for your commitment,
5 for your willingness to be part of this
6 process with us.

7 It is an important aspect of our
8 capital markets and I think we've continued to
9 show a willingness to make what is a good
10 profession even better. So, I thank you for
11 that.

12 Chairman Volcker, anything that you
13 care to add?

14 MEMBER VOLCKER: I don't think so.

15 CO-CHAIR NICOLAISEN: Chairman
16 Levitt, any final words?

17 CO-CHAIR LEVITT: No.

18 CO-CHAIR NICOLAISEN: If not, we'll
19 call this meeting adjourned. Thank you.

20 (Thereupon, at 3:04 p.m., the
21 Meeting concluded.)

22

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