RECORD OF PROCEEDINGS

SECURITES AND EXCHANGE COMMISSION ADVISORY COMMITTEE on SMALLER PUBLIC COMPANIES

Second Day of Meeting
September 20, 2005

10:10 a.m.

The Hyatt at Fisherman's Wharf
555 North Point Street
San Francisco, California

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P R O C E E D I N G S

The following Members were present in person:

Steven E. Bochner

Richard D. Brounstein

James A. “Drew” Connolly

Alex Davern

Joseph "Leroy" Dennis

Janet Dolan

Richard M. Jaffee

Mark Jensen

Deborah Lambert

Richard Leisner

Robert E. Robotti

Kurt Schacht

Ted Schlein

James C. Thyen

John Veihmeyer

Herbert S. Wander

The following Members were absent:

Patrick C. Barry

Pastora Cafferty

C.R. "Rusty" Cloutier

E. David Coolidge

Scott Royster

The following Official Observers were present:

George Batavick

Daniel L. Goelzer

Jack E. Herstein

The following SEC staff members were present in person:

Gerald J. Laporte

Kevin M. O'Neill

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MR. WANDER: Why don't we all take our seats, and we will begin this morning's session.

Welcome to the second day of the meeting of the Advisory Committee and second day of the meeting of the Small Business Forum. We're delighted to have so many of you still here. The schedule for today is that we're going to start off with some introductory remarks by Jim Thyen, and then we will have the presentation of the recommendations of the SEC Government Business Forum on Small Business Capital Formation. And then at 11:15 we're very fortunate to have Larry Rittenberg who's the head of COSO who will present some testimony. We're delighted that he was able to make it out here. And then from noon to about 1:30, we will have a formal meeting of the Advisory Committee. So we'll start off with Jim's introductory remarks.

MR. THYEN: Thanks, Herb. And welcome again. I want to make some comments to give us a little context and perspective as I was in several of the subcommittee meetings, and it seems to be needed at this time. First of all, we'd like to comment now on the excellent meeting yesterday of the Small Business Forum. I think the panel discussions were excellent, the breakout groups added meaning to our work, and the day certainly affirmed the importance of our work and that our work is adjourning. So I want to thank the SEC, Gerry Laporte, Alan Beller for arranging this joint meeting.

And thanks also to Commissioner Atkins for his words. His words were very uplifting and encouraging to our Advisory Committee. Certainly their presence here reinforced their support and their commitment to us in this journey, and it certainly extended a statement of trust that has been granted to us in our leadership. We also would like to thank Marc and Steve for being excellent hosts last night for our dinner.

I think balance, you know, it's a fact of life, and our work balance here is one of the investor protection mandate along with capital formation encouragement. So today we're going to continue the fact-finding journey to seek that proper balance, and we certainly have a distinguished panel that's going to share their thoughts and recommendations with us. We're very much aware of the historical significance of Sarbanes-Oxley, and accordingly, that our work is also very significant. Our opportunity in this journey is a historic opportunity, and we're all very proud to be participants and players in the U.S. public capital market.

Our opportunity is to bring meaningful recommendations to improve those markets and how they are regulated. Those of us here on this Committee are responsible for leading for profit companies, companies that create economic value for this nation. We need three things. We know and we live every day with the reality that economic profit brings economic freedom. It enables us to continue to grow and provide employment and livelihood throughout the nation. For us to keep our economic freedom to remain globally competitive, we need less regulatory burden, less red tape and complexity in compliance, and a lower tax structure. The opportunity of this Advisory Committee is in the first two items. It's the lessening the regulatory burden and lessening the red tape and complexity of compliance.

Our subcommittees are continuing to work very hard. It's clear that we are all very caring and very committed, and we've given a great deal of mind share and thoughtfulness to our work. Now we are starting in phase two. The phases overlap a little bit, but it is phase two of our process journey. Fact-finding is starting to come to a close. We've gathered a great deal of facts, opinions, viewpoints, and recommendations, and now we're starting to move into convergence of our ideas and our recommendations. Now is the time in our subcommittees to refresh your understanding of our over-arching principles. Recall there were five that were given to us by the SEC, and they are published in the Small Business Forum pamphlet that was passed out yesterday.

We as a committee added a sixth one, and it was prioritized recommendations and focus on the top five in each of our subcommittees and in our work.

In March 2005, we adopted our agenda, we adopted our subcommittee end goals and our focus points. Now we are at the time to reach back to those documents and affirm our calibration, affirm our alignment, and reaffirm that we have not missed a key issue in our fact-finding.

A few comments about next steps. We will have a meeting in October of the full Advisory Committee. At that meeting, you should bring your recommendations. And your recommendations should be based on deductive reasoning, not anecdotal. Through Gerry, Gerry Laporte, there is access to a wealth of facts and data. The Office of Economic Analysis of the SEC we have found to be very responsive. They have very bright people, they have a very positive can do attitude. Let's use their skill and their data. They are the bedrock of our deductive reasoning supporting in our recommendations. This is the process that we used in the size subcommittee, and we saw yesterday affirmative statements from Commissioner Atkins that the model works. So let's use that. Gerry Laporte, Cindy Alexander and their staffs are best in class. Just tell them the data you need, ask for their expert analysis of that data, and then construct your deductive reasoning to support your recommendations.

If your subcommittee cannot do that, it is a caution flag to you that perhaps your recommendation needs adjusting or tuning. I think the work of the size committee is a model to follow, and each subcommittee had representatives on that size committee and they participated in that work. So it should be easy to transfer. I believe for recommendations to be meaningful to the SEC, which is one of the goals we set out when we came together back in the spring, our recommendations have to have reasonableness about them. And they have to be reasonable in the context of the SEC's mission. So we need to ask ourselves on the recommendation the question of, "Then what?" If the SEC acts on our recommendations, then what? What will occur? What are the likely consequences? What are the outcomes? And certainly what are the unintended consequences we want to avoid?

Again, the Office of Economic Analysis can be very helpful in modeling the "then what" answer. As we come together in October as a full Advisory Committee, we will need to have confidence in our recommendation, bases in deductive reasoning, and some clarity around "then what." So it's a historical opportunity for us to reduce the regulatory burden, to reduce the red tape and complexity of compliance that are on our smaller public companies. It's an opportunity to strengthen our economic freedom by enabling our smaller public companies to be more profitable and more competitive. To do that we must respect our over-arching principles, we must bring recommendations that are deductive based and reasonable in their outcome and in the "then what" consequences.

We've worked extremely hard for six months, and we are very well positioned for this next phase of convergence and definitive recommendation to the SEC. I hope that gives you a little context, a little perspective about where we're going in our next steps. Thank you.

MR. WANDER: Thanks very much, Jim. And that sort of outlines where we're going to be headed for the next month or so. The next item on our agenda is a presentation by the Small Business Forum. Marc and his colleagues will present their recommendations based on the deliberations we held yesterday. So Marc, do you all want to take -- and my suggestion is that you -- when you make your presentation, that you introduce yourselves, tell us a little bit about you. And I suggest that the Advisory

Committee hold off asking any questions until everybody has finished their presentation. Is that all right, Marc?

MR. MORGENSTERN: That's not only all right, that's exactly what I was going to ask you for.

MR. WANDER: I'm ahead of you.

MR. MORGENSTERN: Good start. As always, Herb.

Following Herb's lead, first let me just say that I'm an attorney and a long-time member of the SEC Forum's executive committee. My focus is on emerging growth companies, venture, private equity, and smaller public companies. So part of the reason why we'll identify who we are is so you can tell where our biases are so you can judge the comments accordingly.

And certainly on behalf of the Forum, we do want to thank the many people; Commissioner Atkins for coming here, we do understand the importance of an SEC Commissioner appearing here, it's very meaningful; the SEC staff, not to single out Gerry and Tony particularly, but we work the most closely with them; the Advisory Committee for coming here, as we also understand the commitment it is for all of you; the Forum participants, who unfortunately are to my back, but many of them come year after year, they are unpaid volunteers, some of them have been doing this for 25 years. It's because they care about small business because they believe it is where job creation comes from, it's because they believe it's where wealth creation comes from, it's because they believe it's where innovation comes from.

The witnesses yesterday, we all thought, I think just as you did, were extraordinary, they were illuminating, they were balanced, and it was hard to believe that people could present such incredibly different points of views so respectfully and helpfully at the same time. This event is unique from our perspective and probably from yours. We have a pattern we follow every year and have been doing that for a quarter of a century. It originally started being described sort of as packwood sessions; you get a lot of information, get a bunch of people together, give them three hours and come up with very specific recommendations. So it wasn't intended to just be a venting session. It was intended to produce product, and product that could be acted on and product that has been acted on over the 25 years many, many times. Sometimes not as quickly as we like, but it gets on the agenda and it gets on the agenda in a respectful fashion.

What happened yesterday from our perspective was classic. We all heard lots of presentations, we got additional data, we then had breakout groups, as you know because you participated, and there were two kinds of breakout groups. We started with a breakout group that included Advisory Committee members that let the Forum participants interact directly with the Advisory Committee, hear some of your history. Jim happened to be the leader in mine and was unusually eloquent and helpful, and Janet chimed in with some comments that sort of let us see the expanded stage you all are playing on, and that was very useful. This group then spent -- and then we had a breakout session that did not include the Advisory Committee members, that reacted to the information that had been given to them, and we came up with two different groups.

One we sort of said our classic recommendations that come out of the SEC Forum, and many of them do not relate to the work that you are doing. Those we are going to take separately, give to the SEC. We only have 40 minutes here with you today, so the recommendations we're going to present this morning to you are those that directly relate to the work that you're doing.

Let me just quickly introduce the people who were the forum leaders yesterday. Lance Kimmel is here. Lance is a securities lawyer from Los Angeles. His focus is on smaller public companies. He's either famous or infamous because he is the author of the Foley and Lardner study. Brian Borders is to his right. Brian is a lawyer in DC, he is the former president of publicly traded companies, he's a former member of the NASD board, he's a long-time SEC Forum participant, and among his clients are the NVCA.

Charles, I actually don't know exactly how to introduce you.

MR. BENNETT: I'm a long-time member of the Small Business Forum and got my start in that when I was the director of the corporate financing department at the NASD department, the department that reviews all underwriting terms and arrangements for public offerings offered by member firms in this country. I'm now a consultant working in the Sarbanes-Oxley area primarily offering software tools and management fund support for corporate governance issues and working in conjunction with another team that provides 404 compliance and internal controls.

MR. MORGENSTERN: Thanks, Charles.

And Ralph De Martino is the vice chair of the securities sect of Cozen, O'Connor in DC. His focus was on audit committee and smaller public companies.

Last night with this group, along with the help of Tony Barone, spent four hours trying to take the presentations and discussions from five breakout groups and synthesizing it into a monolithic presentation. We're going to talk about five or six things. We do want to let you know we have total passion about the first two which are the definition of a smaller public company and the recommendation for finders of the exemption and registration for finders being adopted. We care a lot about the others, but if you're looking for priorities, Jim, in terms of your question, it's one and two, one and two, one and two, and one and two. The rest of them are responses about rule 404, accounting issues, opt out, and I'll let everybody present it. We will try to stay on time. I know that I drive Herb crazy sometimes staying on time, so it will be funny having him on the other side of this. We will be done in 45 minutes. And with that, I'm going to turn it over to Lance to talk to you about definitions.

MR. KIMMEL: Thanks, Marc. Good morning, ladies and gentlemen. The Forum really welcomes the willingness of the Committee to address the fundamental issue of determining which companies should be eligible for consideration for some form of regulatory relief from the current disproportionate burdens that they face in terms of cost of compliance, both in dollars and human resources. We believe that expanding the number of public companies in this group is appropriate to alleviate this burden. We recommend a three tier classification system consisting of microcap companies, smaller public companies, and well known seasoned issuers. The first two categories would be eligible for relief from some regulatory provisions.

We support the use of market capitalization as a good initial criterion for making these classification distinctions. For microcap and smaller public companies, we further recommend that the Committee consider additional measures of size, which we believe are appropriate ways to look at those sorts of companies. We recommend that microcap company, which would be eligible for maximum potential regulatory relief, would be defined as a company that meets any of the following criteria: $100 million in total market capitalization; or $25 million in annual revenues being the current metric for the definition of a small business issuer; or public float criterion based on standards to be established.

We believe that these additional approaches would allow flexibility in circumstances where a pre-revenue or early revenue company has a premium market cap because of perceived desirability in its industry group. A current example of that would be biotech companies which may be years away for their path to revenue, but amply rewarded for what the future might hold. We also believe that public float's an important and appropriate criterion for these smaller companies because that addresses the protectable risk that we believe is an issue, that of protecting public investors rather than founder control public companies that are of an arbitrary size.

We appreciate that the calculation of public float is not as simple and as clear-cut as that of total market capitalization, but we also know that every reporting company every year does that calculation for its 10-K or 10-KSB. To the extent that there's concern that there could be variations in the way public float is calculated from company to company, we believe that a definition of public float could be developed for definitional purposes. We recommend that the category of microcap companies be granted significant relief including, among other things, relief from at least substantial parts of SOX 404.

The second category of company, the smaller public company, is that company that does not meet the definition of microcap and is smaller than a well known seasoned issuer. This group of public companies would be eligible for consideration for scaled regulatory relief. For example, that might include, both with respect to microcaps and smaller public companies, relief from transactional internal controls in return for enhanced entity level controls.

The final category is the largest of public companies using the well known seasoned issuers definition adopted by the Commission in June.

Separately, we recommend that the Committee consider the concerns of the creeping or inadvertent public company and companies with a large number of employees who receive options as part of compensatory arrangements. Some of those issues were addressed yesterday by some of the individuals giving testimony to the Committee. I'd like to add a personal note of clarification, that being with respect to the Foley and Lardner study cited by several members of the committee and one witness yesterday, particularly with respect to the audit costs that were referenced in the study.

In addition to being the author of that study, I was the architect of the study. I created the study methodology, and I personally trained the researchers and reviewed all of the raw data. I would like to assure the Committee that the audit numbers contained in the first annual Foley study were derived from proxy statement data, not CFO or any other estimates. While I'm no longer at Foley, I believe that that methodology has not been changed in subsequent years of the report. I thank the Committee.

MR. BORDERS: Good morning, ladies and gentlemen. I'll be dealing with recommendations number two and number five of our Forum recommendations. The first one should come as no surprise to anyone who's been participant in these forums. It's on finders, or what we hope will soon be known as private placement broker-dealers. Jerry Niesar made a presentation to you yesterday and to the Forum as well on the ABA Task Force report and recommendations on private placement broker-dealers, so I won't bother with details on what the ABA has recommended, but just emphasize that this has been a high priority for the Forum participants for many years. It was the number one recommendation for the past two years of the Small Business Forum. So as Marc said earlier, this is a passionate issue for people here.

Finders, we believe, I've learned from my own participation in these Forums, play an important role in finding capital in capital formation for small companies and the microcap companies. An appropriate regulatory regime for those who perform this function in a legitimate way would remove the uncertainty for these important intermediaries who currently have no regulatory status that fits their own background, their own experience, and the function that they perform. So the Forum strongly recommends that the Committee support this ABA report and recommendation to the SEC.

The fifth recommendation of the Forum to the Committee is with regard to the opt out for microcap companies regarding a safe harbor for microcap companies that have become registered public companies prior to the enactment of Sarbanes-Oxley who have fewer than a thousand beneficial holders and are, in effect, private companies that happen to be registered with the SEC. We believe these companies deserve some form of relief through a mechanism that would allow them to exit their status as public companies in a far more workable and far more efficient manner that is currently available to these companies. Thank you.

MR. WANDER: Brian, would you give us a little of your background?

MR. BORDERS: Sure. My background, I'm a lawyer, I practice in Washington DC. I have been in private practice on my own for about five years now; prior to that I was president of the Association of Publicly Traded Companies; and my clients currently include the National Venture Capital Association. During the last ten years I've served on the boards of National Association of Securities Dealers, now called NASD as, well as the NASDAQ Stock Exchange.

MR. WANDER: Thank you very much.

MR. MORGENSTERN: Charles?

MR. BENNETT: Thank you, Marc, and thank you all, members of the Advisory Committee for having the Forum meet with you in conjunction with this very important work. I'd like to present a few recommendations that we have that primarily revolve around some modifications to Sarbanes-Oxley, and in particular to Section 404. Our first recommendation which has certainly been viewed by this Committee in other forums is that the implementation of Section 404 for non-accelerated filers should be deferred for an additional year. Given the remarks from the commissioner yesterday, we further believe that if the actions taken tomorrow as expected, we further endorse its relief is appropriate for smaller public companies including our microcaps and our small public companies.

We believe it's appropriate that the certification required under Section 404 should not be required of the microcap companies, retaining, however, the certifications that are required under Section 302 and Section 906, to a certain extent relying on the fact that smaller companies have a story to tell that's largely management driven as opposed to revenue and financial statement driven. And we believe that the appropriate emphasis falls under 302 and 906 rather than 404. We also believe that a safe harbor from Section 404 should be created for microcap companies that would permit the use of the single audit standard for 404 attestation including the extent that it's retained as a way of handling 404 internal controls.

We also took a look at the transition roles in anticipation of the fact that the definition of smaller public companies would be adopted. And to the extent that that would be the case, we would view the transition rules as needing to apply across the board, whether to smaller companies currently subject to S-B, larger companies subject to S-K, and well known seasoned issuers or otherwise, the view being that we need to reduce the volatility of those companies falling in and out of the three different categories that have been described as part of the proposal. We believe the SEC, when determining U.S. market capitalization, needs to make that determination as of the end of any calendar year, and to average, several calendar years in order to eliminate the potential for volatility, which certainly would have occurred between calendar years 1999 and calendar year 2002.

We also believe that, likewise, companies, when figuring their market capitalization, should be averaging different time periods so that the point in time calculation that's made is not an arbitrary number, but it is subject to too much volatility. We also reviewed some of the questions around prohibitions for loans that occur under the Sarbanes-Oxley rules and believe that cashless exercise provisions and options that are granted to officers and directors shouldn't be viewed as violation of the loan prohibitions of Sarbanes-Oxley. And that to the extent that indemnification payments in advance of a legal settlement or trial, it would be deemed to be a -- that should also not be viewed as loans, subject to the fact that if the proceeding goes against the individual or the indemnification is used against public policy ultimately as part of the settlement, that those payments would be returned.

We also took a look at the fact that option holders often push people into the category of an inadvertent public company, and we believe that for purposes of '34 Act registration, option holders should be deemed to be a class of securities that would trigger Exchange Act filings and periodic reporting. And last, we looked at the fact that the SEC should consider modifying the going private proposals, the criteria for going private or deregistering a public company under the Exchange Act to adjust for the inflation on the asset side -- it's been some number of years since that threshold's been looked at -- and to shift the predominant means of looking at ownership from record title to beneficial owner reflecting the fact that most securities are now held street name.

MR. MORGENSTERN: Thank you, Charles. Ralph, please.

MR. DE MARTINO: Thank you, Marc. Thank you ladies and gentlemen. The recommendations I'm about to present are specific to the accounting area. There's been much said about the increased cost of Sarbanes imposed on public companies, but I think that one -- and maybe I should go back and state that I represent predominantly small and midcap public companies and I represent audit committees and broker-dealers and am the vice chair of the securities practice at Cozen O'Connor nationally.

So I see and chat with people in audit committees and CFOs on a regular basis, and I would say that in addition to the out-of-pocket cost, probably the most significant challenge presented to them, and I think that cuts across many of the underpinnings of the recommendations made today, is that there is a brain drain. Many of these companies are looking to increase their staffs, not only in numbers, but in capability and are having a significant problem competing with the larger segment of the public reporting market place, and the service providers.

My first group of recommendations relates to the issue of independence. As you are all aware, post-Sarbanes deemed the criteria for assessing auditor independence more, shall we say, heightened or strengthened, and it's led to a series of inequitable circumstances that we believe could be easily remedied and would give great relief to the microcaps and smaller public companies. And let me give you some examples. The predecessor auditor is asked for a consent a year later to the use of its opinion, say, a registration statement context. As part of the termination of the auditor, the auditor agrees to take installment payments. Those payments have not yet been completed. In many circumstances the auditor will respond, "I am not independent; I can't grant that relief. You need to go to your existing auditor and reaudit." It's a tremendous cost being imposed upon these smaller companies.

The second circumstance that we've seen a number of times, and many of the accountants who were in the Forum saw the same circumstance, is the circumstance in which, again, you have a predecessor auditor, it's two years later, and the Securities and Exchange Commission has raised an issue about an item of accounting, say, a beneficial conversion feature. And in the course of the dialogue with the SEC, the company makes a determination that it misapplied the literature. It goes back to its predecessor accountant who says, "Okay. No problem. We'll do the audit, but we need to do our independence assessment." They make an assessment now under today's criteria, and what they find is that, "You know, I think we gave you too much input at the time into this issue, and as a consequence under today's standards, we are not independent, notwithstanding that at the time we issued the opinion, we were independent."

So this public company is looking now at a circumstance where its reports are delinquent, it's being challenged by the Exchange in terms of its continued listing, and it's looking at a tremendous outlay in terms of having that year reaudited by its current auditor. The proposal of the Forum in this area is that that predecessor auditor, provided that he was independent under the rules at the time of the initial opinion, be allowed, one, to issue that consent, or two, to reaudit the restatement provided that, again, he met the independence criteria at the time, and in addition, there is supplemental disclosure either in the notes or in the opinion itself that addresses the issue of independence and the varying applicability of the, shall we say, the predecessor criteria and the current criteria.

MR. MORGENSTERN: Thank you.

MR. DE MARTINO: I'm not done.

MR. MORGENSTERN: Okay. Well, then, keep going.

MR. DE MARTINO: There's been confusion, it was alluded to yesterday in testimony subsequent to the PCAOB's initial statements on this issue regarding the extent to which auditors can speak to or give guidance on accounting literature to their audit clients. I think that the subsequent Q and A that was issued, in my own opinion, is the subsequent Q and A that was issued by the PCAOB clarified the area. But the problem is the accounting profession currently is concerned that anything they do will be perceived as crossing the line on independence. And as a consequence there's been a real absence or quelling of responsiveness, if you will, from the auditor.

This is particularly difficult for the smaller company who doesn't have the technical staff, if you will. And so as a consequence, it's forced to reach out to very expensive third-party providers to get the guidance or finds itself foundering. Our suggestion is that there be further clarification here to make clear to all industry participants, both the CFOs of the world and to the outside auditors, to make clear, perhaps in a Q and A or a hypothetical context, where those lines get drawn. So that the auditors aren't quite so defensive about giving guidance, general guidance on accounting literature, particularly in new pronouncements.

MR. MORGENSTERN: He has more.

MR. DE MARTINO: Almost there. Consistent with the concern about brain drain and consistent with the lack of technical staff that you find in smaller public companies and microcap companies, the Forum recommends that in the event of new accounting pronouncements, take, for example, 123R dealing with options, that microcap companies and smaller public companies be afforded an additional year from the effective date of a pronouncement to implement those pronouncements. That would allow custom and practice, if you will, to become evident, it will allow the independent accounting profession to be comfortable, and it would allow, if you will, the custom -- the accumulated knowledge to vent down, if you will, to these smaller companies.

Finally we believe that in the context of SAB 99, which effectively discusses materiality from a legal perspective, in my assessment, is extremely difficult for CFOs and even external auditors to assess. We find lots of dialogue among lawyers and accountants, internal and external, and many differences as to whether something is or isn't material. We understand the sensitivities of all involved about giving bright line tests when it comes to materiality because, in fact, materiality is ultimately a total facts and circumstances assessment.

But I think that there would be some benefit to discussing materiality in the context of assets, liquidity, earnings per share, those sorts of criteria to get everybody in the market place a better sense of how they should be setting their criteria. The difficulty this gives rise to is the CFO is not comfortable about what is or isn't material, he is, in essence, going to be conservative if he's a good businessman. And being very conservative, he's going to drive up his internal costs and drive up his auditing costs. Thank you for your attention.

MR. MORGENSTERN: Let me just do, Herb, about a 30-second wrap-up before we turn it over to Q and A. Without focusing on any particular recommendation, the essence of the Forum says that small businesses are genuinely different. This isn't just a statutory sort of issue. They have different operating characteristics, they have different capital structures, they have a different use of CFOs, they have a different use of operating personnel. They get penalized because something is material to them that isn't material to their larger competitors, so they have all kinds of anti-competitive features as the consequence of being a public company. They are a different creature.

And as you all are struggling with treating them differently and defining them differently, at least from the small business side, it isn't a game and it isn't a question of statistics, it's a question of considering what is the impact on both the market place as a whole, which is a way of looking at it, but equally clearly on each individual company. Because big companies that large institutional investors would like to invest in don't spring fully born from the loins of Zeus. They have been incrementally going zero to 25 to 75 to 150 to 350. So if you really want a flourishing economy and you really want those large companies, you have to create an environment that welcomes and nourishes smaller businesses.

The reason we said our number one and two priorities, and said differently, the number one, the number one, the number one, the number one, is definition and vocabulary determine outcome. So nothing is more important than that the definition be considered in terms of the audience it is impacting. And while we certainly understand the need for both simplicity and clarity, we equally understand that, as Irwin said so eloquently yesterday, one size really doesn't fit all unless it's men's socks and moo moos. So we do encourage you to look at those definitions and consider the breadth of industries that are being covered by that definition. Think about the examples from this morning of the company with $1 million in revenues but $500 million market cap, they have five employees.

So we just want to make sure that our priorities were incredibly clear. And with that, let me thank everybody here, and then turn it over to you, Herb.

MR. WANDER: Marc, are you going to provide us with written recommendations as well?

MR. MORGENSTERN: Absolutely.

MR. WANDER: I mean, I think it would be helpful. I try to take notes, but sometimes you lose the nuances when you're thinking about the last item that you mentioned. We certainly appreciate all the hard work that you've done in making these recommendations. They are not surprising, by the way, as you can well imagine. We now have about ten minutes or so for some questions from members of the Advisory Committee. Yes, Leroy.

MR. DENNIS: Leroy Dennis. This question is obviously directed toward Ralph since I'm on the auditing subcommittee. You mentioned the ability to allow an auditor to opine on an opinion or reconsent to an opinion if the independent -- if he's not independent today, whether it's because of a lack of payment or because of a change in the rules. Can you address for me how the idea of a matter of emphasis in the opinion stating that the auditor is -- I'm not exactly sure, the auditor's not independent under today's standards would be perceived by the public and we now have a -- in my mind a fairly confusing standard to try to communicate to a public user of those financial statements as opposed to today either you're independent or you're not. I'm just concerned about the effect on a user reading that statement and understanding what they've got.

MR. DE MARTINO: Well, we share your concern, but to some extent, we are narrowing the comment to a circumstance in which the auditor would have been deemed independent under the standards in place, or at least the guidance in place at the time the opinion was issued. And so as a consequence, we have that today. If you look at a 10-K today and it includes 2004, '03, and '02 financials, in essence, the standards that were applicable at 2002 are actually different from those that were applicable in 2004. So while the market is not paying attention to that or maybe hasn't contemplated that, it is there. So we're suggesting that with some good hard work, that could be articulated.

In many of these circumstances, we're talking about years, going back three and four years, and one would argue that the effect is not -- may not be, depending upon the facts, material, but technically we're obligated to have three years' audited financials, technically we've discovered an error, and technically under the literature, we're obliged to restate. So, you know, we're in an environment today, with my deference to my SEC brethren, that practically every error that results in a change is presumed to be material.

MR. DENNIS: If I could follow up, Herb, I wonder, as opposed to a different standard for independence, if some kind of de minimis rule that would allow some sort of judgment so it's less black and white. I'm troubled by if we have an auditor having to redo work or reaudit, I mean they are auditing today and they're not auditing two years ago, and so I'm struggling with how to get to your position. Now, if I had a situation where it was a fairly immaterial circumstance or something that was de minimis, then I could much more easily get to that position that you're in. We struggle with this in our committee, we actually have very lengthy discussions about how to get -- how to overcome some of these circumstances, and quite frankly, are struggling with communication and with how we would make that work.

MR. DE MARTINO: Well, you know, I might suggest that a variation on your theme might be that the auditor -- the financials are deemed audited, if you will, except to the extent of the restatement, and that there be some relief given to smaller companies with respect to the audit of the restatement itself. I'm talking about a circumstance where the restatement doesn't have far ranging effects on the income statement and balance sheet.

MR. DENNIS: So allowing the -- in your case, the current auditor to audit the restatement?

MR. DE MARTINO: Correct. Limited to the restatement.

MR. DENNIS: That can be done today, I believe.

MR. DE MARTINO: No, that's limiting it to -- the problem with that is that today the current auditor's going to say, "I need to go and reaudit everything." So if your audit fee is $400,000 a year, it's most likely, since he's going to have to get comfort on opening account balances and do that audit as if it hadn't been done before, so to speak, with whatever reliance he can give to the prior work, it's going to be a very expensive engagement.

MR. DENNIS: Okay. Maybe what we can do instead of tying up the whole committee here, sometime you and I could talk one on one on that.

MR. DE MARTINO: I'd be happy to reach out to you.

MR. DENNIS: There's a lot of issues that I struggle with, and so maybe we can get together on that.

MR. DE MARTINO: We would be eager to discuss.

MR. WANDER: Ted?

MR. SCHLEIN: In the spirit of definitions as being one of the major concerns, Lance, I go back to you. You're very clear in defining what a microcap was metric-wise, and maybe I missed your definition of the smaller public company with the same precision of metrics. But do you have a recommendation -- does your group have a recommendation as what would define a smaller public company in terms of revenue, market cap, public float, as well?

MR. KIMMEL: To avoid any gaps in the definitions, that would be, in essence, the default definition. You have a defined microcap, you have a defined well known seasoned issuer. If you're neither of those things, you are a smaller public company. It would pick up the span between those two categories.

MR. MORGENSTERN: And also self-calibrates, which is one of the Advisory Committee's stated goals.

MR. SCHLEIN: Right.

MR. WANDER: Yes, Steve.

MR. BOCHNER: This is to Ralph on materiality. I do think we're in an environment where when in doubt, you restate. It's almost an over restatement environment where restatements come out and the shareholder reaction sometimes is, well, why are you restating this? Isn't it material? And I'd like to see if you can get a little more granular with your recommendation for us on materiality. Are you talking about an exception or revision to SAB 99 so you wouldn't be thrown into sort of a case law environment but lawyers wouldn't be deciding materiality issues and you could actually have a bright line test for purposes of financial statements only, or are you talking about something additive to what's already in SAB 99, which is kind of a facts and circumstances, reasonable investor sort of test?

MR. DE MARTINO: I think that's a good question. The thinking is that SAB 99 is a fair and complete summary of the case law, with an accounting bent, if you will. The problem is that accountants are not lawyers. And that we are not suggesting that SAB 99 be rewritten, so to speak, because that would really encompass rewriting the law, if you will, on materiality. Rather we're suggesting that there be specific Q and A type guidance, hypotheticals that highlight other considerations, that highlight sensitivity to earnings per share, that talk in terms of liquidity or percentage of assets, percentage of real versus intangible, those sorts of assessments that we all deal with in this context. Nothing would be definitive, but it would give, I believe, financial professionals a better footing to understand what it is they're really dealing with in a financial context.

MR. BOCHNER: Would you think an alternative to that could be a definition of materiality just for financial statement purposes that would not be binding in terms of MD & A and, you know, for general disclosure purposes, just so accountants and their clients could determine materiality in the financial statement context without seeking input from the lawyers on whether to restate? Or would you prefer the environment we described which is just kind of adding to SAB 99?

MR. DE MARTINO: I think the financial professionals and accounting professionals would embrace that. We were hesitant to recommend something like that because, frankly, we were not sure that that was a viable proposal.

MR. WANDER: Yes, Drew.

MR. CONNOLLY: Mr. Morgenstern, I want to both personally thank you and I think institutionally thank you for being the eminence gris of the SEC Small Business Forum on Capital Formation. I know in the four years that I've attended and participated, I've welcomed your wisdom and input. And in that regard, I think I'm mindful of your comment which parallels one that I've made relative to inside every microcap CEO, there's a mid cap or a small cap waiting to break loose. And the truth is that the only way that we can encourage in this country both the market capitalization growth and presumably the profitability, the ability to compete in that global market place, add jobs, and contribute to the economy is to find ways to assist with the removal, if you will, or the right sizing, of the regulatory burden.

And I think that in large measure, we have adopted or will be hopefully adopting -- and I know my Subcommittee on Capital Formation finds your number two to potentially be our number one, and finders is very much on our minds. And I can inform you clearly that state securities commissioners are looking at it very seriously and I know the Commission itself is. So I wouldn't be surprised if that perks up to a solution.

MR. MORGENSTERN: That would be great, and you know the Forum would be incredibly grateful.

MR. WANDER: Any further questions or comments? Janet?

MS. DOLAN: This is Janet Dolan. I just have to ask Mr. Bennett for a clarification. I may be suffering from what Herb said, writing when I should have been listening. But would you tell me, just describe a little more fully the safe harbor that you're looking fur?

MR. BENNETT: And I may have to reach out to some of my panel members. This particular safe harbor was developed in another breakout session that I didn't attend. But as we understand the concept of a single audit standard, we're looking to allow the audit firm that's not only doing the financial audit, but it's also doing the internal control audits to be able to combine those two more effectively and, thus, reduce costs and overhead.

MR. KIMMEL: That was my breakout group that discussed that, and I think that's an accurate description that Charles has given.

MR. JAFFEE: Herb?

MR. WANDER: Yes, Dick.

MR. JAFFEE: I want to come back to the size issue and just make a couple of quick points. First of all, I think somebody's already clarified that you accept the safe calibration and the size would be based on the percentage of market capitalization, not these absolute numbers. So for ease of conversation, we use the term 100 million, but we really don't know whether it's 120 or 89 or something like that.

In terms of the float issue as opposed to total market capitalization, Jim knows that sort of late in the game I woke up to the fact that that was a real issue. And that I asked that Kevin to provide me with some information from the Office of Economic Analysis which I just got this morning, which sort of confirms what I intuitively thought that there's about a 30 percent difference between the two. In other words, if you have 100 million total cap, on average you've got about 70 million total public float. And so I think that that really is an issue that we need to focus on and come to some conclusion about. I'm going to ask Kevin to provide this to Jim and Herb because I just got it this morning. I haven't had a chance to give it out.

I agree with your position on public float as a relevant metric. And then finally, just to sort of state the obvious, you made some reference, Lance, you did, to some possible relief at these various levels. I would assume, and maybe I'm making a false assumption, that if our Committee granted greater relief that you mentioned, you would not be unhappy.

MR. KIMMEL: I think it's fair to say that the Forum would be very pleased.

MR. JAFFEE: I just wanted to get that out of the way. Okay. Be bold.

MR. WANDER: All right.

MR. MORGENSTERN: Actually, "be bold" really is the bottom line. What you guys are doing is going to effect this country for 20 years. It is not the time to be timid and take the easy way or statistically valid way. It really is an opportunity to say we have two different groups of folks, we have active regulatory and economic reasons to treat them differently, and we're going to just say they're different and recognize their differences.

MR. WANDER: All right. Well, we've run out of time. Marc and Ralph and Charles and Lance and Brian, we thank each of you. We collectively thank the whole Small Business Forum for your recommendations. And as I said earlier, nothing was new or surprising.

MR. MORGENSTERN: Thanks for the opportunity.

MR. WANDER: So we will very carefully consider them.

The next item on our agenda is to hear from Larry Rittenberg who is the chair of COSO. And while Larry is walking up to the table, I will just say that I had the pleasure of meeting Larry, I guess it was two weeks ago in Madison and found him to be not only extremely knowledgeable about the whole accounting area and 404 and COSO, but also a very charming person. And so Larry, we thank you for taking time out of your extraordinarily busy schedule to come and visit with us and to provide us with an update on what's going on with the COSO committee who is considering relief for smaller public companies. And also we did submit to Larry a series of questions, which hopefully we'll get time to discuss with you. So the floor is yours.

MR. RITTENBERG: Thank you very much, and thank you for inviting COSO to present before you. As you know, I did receive a series of questions fairly late last week so that I was not able to submit responses to those questions in advance. However, I did prepare them, and I did prepare two things. Let me talk about what they are. The first is sort of a quick summary of a number of activities that COSO has been involved with over the years and the stances that COSO has taken. Second one is specific answers to the questions that you have addressed. And I can hand them out now or I can hand them out when I'm done. I am going to try to cover most of the points in there in some brief opening remarks.

MR. WANDER: Why don't you pass them out later, Larry.

MR. RITTENBERG: Okay.

MR. WANDER: Then we won't have people fumbling through them and distracting away from your presentation.

MR. RITTENBERG: Okay. Thank you very much.

What I'd like to do today is essentially four things, and I am going to try to keep my remarks fairly brief because I know that you have a number of questions for COSO and where we are on the current project. So what I'd like to do is to present a very brief history of COSO, talk about the composition of COSO, and I would like to very quickly review some of our major publications today. I'd like to give you a brief update on our current project, and then I'd like to give you sort of a top level response to the questions that I received last week.

COSO unfortunately goes by its acronym, the C-O-S-O, which stands for Committee of Sponsoring Organizations of the Treadway Commission. Now, the sponsoring organizations are the American Accounting Association, the American Institute of C.P.A.'s, the Financial Executives International, the Institute of Internal Auditors, and the Institute of Management Accountants. The organization came about in the mid-1980s when those five organizations became concerned with the amount of fraudulent financial reporting that was taking place in our market place. They came together to form the National Commission on Fraudulent Financial Reporting, here and after and mostly known as the Treadway Commission. So that's why we are the Committee of Sponsoring Organizations of the Treadway Commission.

Since that period of time, COSO has issued five major reports. The first was the National Report on Fraudulent Financial Reporting. That led directly to the area that I believe we want to discuss most today, and that was the development of the internal control integrated framework. Following that, we were asked to provide additional guidance related to derivatives, usage, and organization. We followed that up with another very interesting study that looked at accounting and auditing enforcement actions taken by the SEC during a ten-year period from 1987 to 1997 to look at what the impact was in the current state of fraudulent financial reporting during that period of time. Late last year we issued an enterprise risk management integrated framework.

I'm only going to highlight a couple of these right now. The major one was the National Commission on Fraudulent Financial Reporting. What I found interesting, and I was not a member of COSO at that time, is as I have used that report over the years in classrooms and major discussions, is that the recommendations in that report really parallel, both in written word and in spirit, many of the items that were enacted into the Sarbanes-Oxley bill of 2002. For example, it talked about areas such as the need for more vigilant audit committees, the need for the audit committees to really be the external auditors' client, the need for greater management oversight and responsibility for internal controls. It did recommend at that time a management report on the effectiveness of internal control.

And it did suggest that we change the way in which auditing standards are set. It did recommend that the composition of the auditing standards board ought to be changed to have more non C.P.A.s and to reflect the public interest a little better in the setting of audit standards. I think those are all interesting coming from five accounting organizations, those kinds of recommendations. They also recommended that at that time that we needed to develop a comprehensive integrated framework on internal control. And for those of you who are my age, you'll recollect, and if you've looked at internal control methodology at that time, there were a series of checklists. And each company had its own checklist, and they weren't necessarily comprehensive, and they did face, or focus primarily, on controls over transactions.

So COSO undertook that engagement and in 1992 issued the internal control integrated framework. I believe that that framework was unique for its time and certainly different from existing practice in three fundamental ways. One, it is a framework that is comprehensive. It is comprehensive in that it includes objectives related to operations, financial reporting, and compliance. And it does believe, and it did believe, that efficiencies are gained when an organization looks at achieving all three of those objectives. It also views internal control as an integrative process that starts with control environment and goes through or incorporates all five major components of the control framework: the risk management, the control procedures, monitoring, and information.

And then third, and this is some area perhaps of some concern, it is a principles based framework. It lays out the fundamental principles of internal controls. And I believe that that is a real strength of the internal control framework because best practices in specific control procedures do evolve over a period of time. If we were to look at best practices for the engagement of an audit committee in 1992, we would understand that they are much different than what we assume best practices are today. However, the principal that there ought to be effective oversight by the board of directors in an audit committee is established in the fundamental framework in 1992. That framework is designed such that all of the components are supposed to work together to address the risks that the organization faces. Taking one by itself, we believe, is a bit risky.

The second COSO report that I want to focus a bit on is the report on fraudulent financial reporting. And I will note that I have included the summaries of both of those reports in this document here that I'll hand out. That report was a follow-up to the Treadway Commission. We engaged three independent academic researchers to look at actions taken by the SEC during the 1987 to 1997 time period. They identified approximately 350 such actions and focused on a sample of 200. Of those 200 that they focused on, I think these statistics are relevant to the Committee, 78 percent were on companies that had less than $100 million in revenue. Also in those cases, the CEO was involved in the fraudulent financial reporting in 72 percent of the cases.

I contacted all of the authors of that study to find out if they had done any further work, and there is a study currently underway by Joe Carcello, who's at the University of Tennessee and one of those three members, and they're looking, again, at AAERs from 1998 through to 2003. They found approximately 160 accounting and audit enforcement actions taken during that period of time. And what, again, they show is that the bulk of the actions are taken against companies that would fit your definition of smaller businesses. So I think that that continues to be relevant and continues to be a concern.

Now, regarding our current project, we started this project in February of this year based upon some conversations we had with Don Nicholaison at the SEC. I wish we would have started earlier, but there were some reasons that we didn't get started until February. When we talked to Don, his major requests were that we develop guidance that would assist small businesses in better implementing the COSO framework. As we did that, we took that literally and said it was not our objective to develop new standards, we did not feel there was a need to develop new standards, but there was a need for clarity on the existing internal control framework.

So during that period of time, we met with various constituencies including the SEC, the PCAOB, we formed a broad task force. We had a forum in which we invited preparers, some users, and a number of auditors to identify issues that are unique to small businesses and issues that they believe we ought to cover in our report. We have called out on a number of occasions for examples of either controls or risks that are unique to small businesses. We have focused on providing clarity to companies in implementing the internal control framework. The last item in this particular document that I've prepared outlines 25 basic principles that underlie the internal control framework, we identify attributes of those principles, and we provide guidance to smaller businesses as to how they might implement it.

Our current project contains both the identification of specific approaches that a small business may take as well as real world examples of approaches that small businesses have taken to achieve internal control. We expect that to be ready for public examination fairly soon, and I would certainly love to share our results with your Committee and to get feedback from your Committee, if you would like to take a look at it. We do believe that it will help the companies in reducing their costs, but it is not going to be perceived, in my view, in the market place as a panacea. We did not invite COSO -- or invent COSO Light. We don't believe there is a COSO Light. It sort of reminded me of when I took a brief walk this morning, probably some of you made the same walk, but I went down a couple of blocks and I saw the sign that says, "Free crab cakes, tomorrow." All right? We feel somewhat the same way about internal control, although we have tried very much to identify ways in which smaller businesses can achieve the objectives in internal control in a much more cost efficient manner.

Let me give you nine quick responses to some of the questions that I received last week. One related to public reports on internal control. I need to go back and reiterate that the Treadway Commission in its similar report on fraudulent financial reporting recommended public reports and internal control when it was issued in 1987. I do believe that the other reports that I just described in progress, looking at enforcement actions from '87 to '97 as well as one currently underway, does not provide support for a conclusion that smaller companies should be exempted. We believe, and the Treadway Commission points out, that there is a compelling case that there are significant benefits associated with better internal controls. And I do believe that it's going to take some time for us to fully realize those, and I can talk a bit more about them later.

Requiring management assessment and auditor reporting puts teeth into good internal control. We had had something like that earlier such as the Foreign Corrupt Practices Act, but it seems that that did not have the teeth to essentially get everyone's attention. However, we do agree with much of the testimony that I know you have heard during your committee processes, that the costs are high and the costs need to come down. We need to understand first why are the costs so high, and I don't think we have a perfect understanding of that. It is said that the costs are so high because there's too much emphasis on documentation and testing, and there's too much rigidity in the auditor's procedures. But there are other reasons that could equally explain.

For example, there are poor or non-existing controls in some of these organizations. Companies have not standardized their control procedures. Companies have not leveraged information technology to increase the effectiveness of their controls. We also believe that there can be some efficiencies in the future related to controls. For example, I personally am a large proponent that we can move to more effective monitoring controls, who we can monitor the controls and rely upon monitoring as an effective approach only when we have established a bench line for effective internal controls.

I used the example a couple weeks ago when Herb and I were at the same conference, it sort of reminds me when I turned 50 and I went in to the doctor for a physical. He wanted a benchmark to establish how things were so he could monitor my physical health after that period of time. All right? To the same extent, companies need to establish a benchmark for the quality of controls before you can rely on monitoring as an effective control to ensure that the controls are continuous and are adequate. So we believe that controls will improve and the costs will improve or decrease over a period of time.

Point three, internal controls ought to be built into the fabric of the organization. Individuals ought to assume responsibility for those controls. Controls ought to operate on a continuous basis. Therefore, as we've examined one of the recommendations that internal control should be evaluated or reported on every three years, we feel that there may be some dysfunctional aspects with that recommendation. One, it sort of postpones the idea that it has to always be built into the organization. There may be the tendency to defer maintenance or investment in the control structure over that three-year period. And I have heard in a number of comments here that we should all understand that investments in small companies are risky and that the investor knows and should know that those investments are risky. However, just because those investments are risky, we do not see that as an excuse to eliminate some of those risks by requiring better internal controls and more transparent financial reporting.

A fourth and, I think, an important element for your committee is we believe that small businesses can and should tailor internal controls to their organization. We point out in the project under way that there are many instances in which it can be tailored in a much more informal manner so that we can rely on informal controls and we provide specific examples. We also talked about complexity and sophistication, one of the areas you had a question on. And our approach is to understand that complexity and the sophistication of controls tends to mirror the complexity and sophistication of the transactions into which the organization enters. If a company is fairly generic as simple operating procedures, it can have fairly simple controls. However, if it is speculative, if it invests in various forms of derivatives, then it needs more complex controls.

So complexity relates to the nature of the organization rather than just the size of the organization. The same thing regarding documentation. The documentation that is needed depends on the need for public reporting and both the value and the complexity of the transactions and the processes. For example, we point out in some ways, and I'll use a simple example related to instituting the code of ethics, it doesn't have to be signed by everyone. It could be posted on the workshop floor. Management could indicate in various documents including the personal calendar that they have given talks related to the code of ethics and have reinforced it by various actions. We also talk about and believe that small businesses do find ways to effectively compete. And we identify areas related to controls where they can compete effectively such as retainer agreements for accounting advice, outsourcing perhaps some of the monitoring through an internal audit activity, and receiving advice where permitted under professional rules by their outside auditors.

Fifth, we do believe that monitoring should assume a more important role as we move forward. If we look at the COSO internal control integrated framework, it does say that once an organization has implemented effective internal controls, that they can monitor the effectiveness of those controls by either continuous processes or by separate evaluations. Monitoring that identifies deficiencies in controls and takes prompt action to fix those controls, we believe, can be very effective, and may eliminate the need to independently test all of the controls each year, again, once the benchmark has been set, once we understand that an organization has effective controls.

Another question I received related to the practicality of the guidance that we're going to prepare. Our intent is that it's going to be practical and it's going to be useful. However, having said that, I think it is important to understand that implementing effective controls requires thoughtfulness on the part of the individuals implementing those controls. In other words, controls exist to address specific risk. If you identified the specific risk, then you need to think about what kind of control procedures specifically address those risks. It may not be the same answer that you would get if you simply checked off an internal control questionnaire. We are going to, however, provide a questionnaire that's based upon the principles that we developed, and we believe that it will be effective in helping an organization organize its assessment of controls.

One of the issues that you are talking about is a new model called a control environment model. I have read a bit about it, I would say that I probably am not fully versed on all of your thought processes regarding that model. But from what I've read, let me give you the following comments on that proposal. First, as COSO views internal controls, it is an integrated framework where all of the components are expected to be working. We think that the control environment by itself is more difficult to evaluate than other parts of the control model. I think we have seen history shows us that we can often be fooled by a very persuasive CEO whose intentions and whose rewards are built on other things than effective and transparent reporting.

We believe that a control environment should be corroborated by the effective implementation of controls. We also recognize that the control environment, as strong as it may be, does not by itself ensure that the controls over transactions, accounting estimates, or adjustments are going to be effective. And again, there are many reasons for that. People make mistakes, computer systems may be subjected to viruses, one bad person may have different kinds of objectives. So in our view it's an integrated model. The control environment must be corroborated by active control procedures.

Further, as we understand the proposals for an integrated audit, I would point out that the nature of an integrated audit says that what an auditor does is to identify the weaknesses in the organization's control structure. Those weaknesses mean that certain types of errors or irregularities or misstatements may take place. Once you understand those weaknesses, the audit procedures need to be developed to address those specific weaknesses. And I'm not going to go through some examples on that, but I would point out, in a simple area such as dealing with receivables where there are weaknesses, that a standard extension of substantive testing, which is one to send out more confirmations, would not be very reliable in detecting all of the misstatements in the account balance. All right. Just a short example, and I can elaborate on it off-line if you would like.

Further, I think I would caution one of the statements that I've seen in the sense that an absence of errors in the financial statements does not lead to the correct inference that internal controls are effective, nor that internal control will prevent a major fraud or misstatements in the next period. We have seen many smaller businesses that have had inadequate controls, let's say, due to segregation of duties, and have not had any errors. Right? It does not mean, though, that they would not have material errors in the next year should that person with incompatible duties have a personal financial crisis. Right? And find that they can selectively borrow money, at least in their minds, from the organization.

We do think that we are in the early stages and it's much too early to abandon the internal control integrated framework. Our exposure process is such that we hope to have our exposure draft ready by the middle of next month. As I indicated, I'd be happy to include all of the members of the Committee on our mailing list to receive a hard copy of that. We plan to expose the document for approximately 60 days. There would be some time for us to digest the responses, and our hopes are to issue a final document in the first quarter of next year. At this time we do not plan on public hearings, but we are open to the suggestion and we may reconsider depending on the nature of the comments that we receive back.

Now, that's a broad overview. I want to reiterate from our point of view that COSO is very committed in working with the SEC, the PCAOB, the GAO, and your committee. There are questions about what we need to coordinate, what we should do in concert. We are open to your suggestions and we want to be a positive contributor to the work that you're doing. Our objective remains to assist organizations in approving their governance, risk management, and control processes to mitigate the likelihood of fraudulent financial reporting. That's the end of my prepared remarks, and I'd be glad to take any questions that the Committee may have.

MR. WANDER: Thank you so much, Larry, for really spending the time to organize all your thoughts in response to our questions and to give us a view of COSO. I'm sorry. You're in the sun. Do you want to move?

MR. RITTENBERG: That's okay. That's fine. Thanks.

MR. WANDER: Before we start with the questions, I should alert you to the fact that yesterday Lynn Turner was one of our presenters. Lynn produced a, I guess, 168 page submission. But one of the documents that he submitted was a questionnaire that Glass Lewis prepared, Appendix B to his submission, and I can make sure that you get a copy. And the interesting fact was he said that a CFO should be able to answer the questions in one day and the 404 audit should take one week. I think I'm summarizing his comments accurately. And as you know, Lynn is a strong supporter of internal controls. But at some point, I'd love to hear your views, after you get a chance to look at his questionnaire, and assess whether it works, and secondly, whether it works in the time frames that he mentioned. In any event, that's something for you to --

MR. RITTENBERG: Well, I have seen his questionnaire.

MR. WANDER: Oh, you have. Okay. We're open to questions.

MR. RITTENBERG: If I might quickly respond, that questionnaire really is based on what was developed in Coopers and Lybrand shortly after the issuance of the, as I understand it, the internal control integrated framework. I think it's a good start, I think it has provided an impetus for us to even develop a much more detailed questionnaire. Personally my reaction, and I don't think further thought would change this, a statement that it would take one day or one week, without understanding the context or the size of the company or its operations? I think controls are tailored to the organization. I think it simply can be efficient and more efficient than it has been from a time frame. But to come with a specific statement that I believe it would be one day or a specific company just doesn't coincide with my understanding of the processes.

MR. WANDER: Okay. Thanks very much. And now we're open for questions from members of the Advisory Committee.

MR. JAFFEE: I have one. First of all, Mr. Rittenberg, I got a degree from your eminent university, a long time ago in the accounting department. So I'm glad to --

MR. RITTENBERG: We're pleased.

MR. JAFFEE: You know, the -- and I am somewhat familiar with the COSO framework. I serve on the audit committee of a large financial services business, and the Treadway Commission, COSO framework is something we focused on. And I guess my comment is that I agree with much of what you have said in terms of the importance of internal controls and having a coordinated comprehensive framework in which to implement them, but that doesn't seem to be exactly what we have been struggling with. What we've been struggling with is the implementation of 404 and the cost and trying to measure that cost against what we perceive to be as limited benefit. So if we -- if the general question was should small companies have better internal controls and follow the very thoughtful process as the COSO Commission has presented it, I'd certainly be in favor of that.

But there's sort of a presumption in what you've said, which I guess I just don't agree with, that the implementation of 404, as it is presently being implemented, will deliver significant benefits in terms of avoidance of fraud or even an avoidance of material misstatements in financial statements. I think from what I've heard from my organization, there is so much focus on small transactions and documentation and so much misinformation about what really is an appropriate comprehensive framework of internal controls that I'm beginning to believe that it's almost going to be counterproductive. We're all going to end up with a worst system by the implementation of 404.

I know I'm making sort of a long statement here, but I agree with what you said. If we could really tailor-make internal controls to a specific company, looking at materiality, looking at risk where these individual businesses have it, I'd be all in favor of it. But that just doesn't seem to be the way this thing is going.

MR. RITTENBERG: I think what your statement says is that we all have to work on better implementation of 404, because I think your observations are correct that there has been almost an over tendency to focus on items that are not material and that there's been an over tendency to focus on documentation to the nth degree. While that's all true, there may be one silver lining to that. And that is if a company, in fact, does document and they decide what is really important and they focus on what is really important and they develop mechanisms to monitor the working of those controls after year one, then we can and should have more effective implementation of internal controls and monitoring controls and that should be much less costly to those organizations.

I think it's important to recognize that COSO does -- or has as one of its major elements, effective monitoring controls. So while I tend to agree with you, there's been too much done, it doesn't mean that there can't be long-run benefits. But we have to sort of calibrate what we're doing much more effectively. And I think the guidance that the SEC and PCAOB has tried to give us on focusing on risk and integrating the audit is a step in that direction.

MR. JAFFEE: Well, I think you and I agree. I think it's the accounting firms that need to be brought along.

MR. WANDER: Leroy, and then Alex.

MR. DENNIS: Leroy Dennis. Thank you, Larry. I just had a question. You cited a couple statistics that were very troubling and one was 78 -- I think 78 percent of fraud occurred in companies under 100 million in market cap, and 72 percent of those involved the CEO. Just a couple questions around those, have you, in your statistics, done any study as to the dollar amount of that 72 percent or 78 percent versus the 12 percent of, I assume, over a hundred million? And the second question is has there been any studies of the 72 percent that involve a CEO, would the COSO framework or the SOX 404 requirements have detected those frauds on an earlier situation than what they were?

MR. RITTENBERG: Those are great questions. Regarding the first question, it was 100 million in revenue rather than market capitalization that we referred to. There are some statistics, and I believe they're included in the summary that I put in here, they are in the overall document. And I don't quite recall what those are. But certainly in some ways, the dollar amounts are certainly much smaller than the major frauds we've had in the last few years.

The question, your second one is really significant and deserves more research on our part as well as others, and that relates to whether or not an examination of the control environment itself would have led to identifying higher risk and would have detected that. Now, my understanding of audit standards is, as they existed at that point in time, required that, and yet they were not detected by the auditors and the subsequent testing. I think it's important to understand that while we focus -- and this is my personal view rather than COSO's view. That while we focus on 404, that 404 is part of a much broader package that I believe is aimed at curtailing the amount of fraudulent financial reporting. That includes changing some of the independence rules as to who the auditor is responsible for. I certainly noticed -- I also serve on a board -- that clearly the audit committee is the client today, and that drives a lot more activities. And as we convey our sense of risk, the auditors are quite responsive. But I'm sorry that I do not have research that answers your second question, and I think it's a very pertinent question.

MR. WANDER: Alex and then Janet.

MR. DAVERN: Leroy's question actually plays into what I was going to comment on. I just wanted to add a couple of comments and then perhaps such some data that COSO framework could take a look at relative to answering Leroy's second question. Firstly, the comment about 78 percent of frauds being in smaller public companies based on, I guess, data that was gathered from '87 to '97.

MR. RITTENBERG: Yes.

MR. DAVERN: In our definition of how we define public companies, it's very difficult to match up the two sets of data because I don't have the basis of size that you used at the time, but we're covering about 80 percent of the public companies. And so I want to make sure that before we leave a lingering perception that financial fraud is more prevalent and disproportionate in smaller companies, that we have data to support that, that clearly shows that because I have not seen that to date.

The second, I think I would like to address or perhaps offer as a source of information to COSO that I think would be very valuable, and obviously you're speaking as a representative of these five accounting organizations. My constituency I represent is the American Electronics Association, which is about two and a half thousand electronic companies in the United States, and obviously a very different perspective. So with that being said, there is a wealth of data available on the effectiveness and lack of effectiveness of internal controls at detecting fraud by C-level officers. There's the association called the American Association of Certified Fraud Examiners that produces an annual report on fraud and occupational abuse in the United States. And this was included in an AEA white paper which was submitted to the Committee back at the very beginning of the proceedings in April.

And what that shows is that for frauds committed, financial frauds committed by owners and executives, tips, i.e., whistle blower type activities account for 51 percent of the detection of the fraud; regular internal audit procedures account for 23 percent; regular external audit procedures of the financial statements account for 27 percent; and 12 percent are accidentally detected; and 5.9 percent are detected by internal controls. Now, one of the things that I learned in my first year in accounting school that was taught for us and also when I joined a Big Four auditor and went through their initial training is that frauds caused by collusion by senior executives are very, very difficult to detect by internal controls.

The basic premise is, I've always understood it at internal controls, is some person does something and some additional person checks what that person did to make sure it's accurate. And I think that's the fundamental premise of internal control. And when I look at that, I think that internal controls are very effective at detecting honest errors that are made at different levels of the organization by enforcing that review. But I think it's inherently obvious that if the two people who are the doer and the checker get together to commit collusion and fraud in that manner, that the internal control would be signed off and the review would be completed and the signature will be in place, but that is no effective prevention against the fraud that's being committed.

So I'd like to really encourage the COSO committee, when we look to discussing financial frauds and discussing effectiveness and benefits, to really challenge themselves to examine the realities of whether these frauds will be prevented by internal controls. And I site particularly Enron as an example. The last report I saw said that 39 people were indicted by the various different authorities in relation to the Enron accounting scandal. And that's obviously collusion of some form or another that reached to pretty high levels. I have seen several reports that have determined that that would not have been prevented by 404 and internal controls. And I have not seen anybody put forward any solid case that convinces me that 404 will prevent those frauds.

And to finish my statement and look for a response from you, as a CFO of a large public company, not a small public company, but a large public company by our definition, and as audit committee chairman of a large public company, my personal belief is that 404 in my company will not make it any more difficult for C-level officers to commit fraud if they so choose. So I really would encourage you -- I'm going to send you an e-mail copy of this report. I think it would be useful reading. And I urge the COSO group to really examine the linkage between the successful detection of financial fraud with internal controls as they go forward with their examination.

One last piece of data I would like to share, and I think it might be useful again for the COSO group to consider, is this issue of the hope that the cost will come down in year two or year three as these things mature. Now, we had to hope that this would cost $90,000 per company, but that didn't turn out to be right. A recent survey just completed by NASDAQ and the American Electronics Association, to be published later this week or early next week, we got responses from 300 companies and we did this survey in August, several months after the new guidance was issued. The good news on that survey is 80 percent of companies are aware of the new guidance, and about 80 percent have discussed it with their auditor. The bad news unfortunately is the expected weighted average reduction in cost in year two is only seven percent.

So we'd really like to also have COSO seriously considering and examining the recommendations. We need to move beyond, I think, the hope that things will get better and really face the fact that that may not happen. And if it doesn't, that we may need some more robust framework that will really provide a solid framework for smaller companies to use in their approach to 404. I realize I've made several statements and not asked many questions, but I'm curious as to your response to those various statements.

MR. RITTENBERG: As I get older, it's hard to remember all of the questions -- let me try to respond at least to some of them. I am familiar with the certified fraud auditors, and I regularly read their reports to the nation. As I understand in terms of the timing of when the last one was issued, it was before Sarbanes-Oxley all went into effect since the controls have been implemented. I could be wrong on that. But, you know, their findings for the most part were before Sarbanes-Oxley, and it takes a while to get many of these items implemented. Regarding the issue of collusion in the C-suite. If we look at collusion in the C-suite, and one of the points that I actually have in my written comments is that what allows a lot of that to happen is the weaknesses in the basic control processes.

Instead of Enron, I'll take WorldCom for an example. Certainly we did have problems with the tone at the top. But we also had problems in basic journal entry submission and review and analysis by both competent internal personnel as well as external auditors. So if you look at the total of the concept of internal control, it talks about a commitment to competency and that there is independent review. If you look at Enron, for example, the chair of the audit committee had been chair for over 20 years. You may ask some questions of whether or not there was an effective oversight by the audit committee, especially when the audit committee explicitly approved the series of SPEs that Enron engaged in.

Regarding the cost, my comments were not based upon a hope, per se, but sort of a logical extension and implementation of COSO framework. That all said, I would still be happy to have you share your information with us, and we will examine it in more detail.

MR. WANDER: Janet?

MS. DOLAN: Yes. Thank you for your testimony today, Mr. Rittenberg. I have a question for you, which is I hear some of your statements today that COSO can be tailored depending upon the size of the company, that informal controls should certainly be adequate for small companies. You're saying all the right things, but we have heard from a lot of auditors in this process, and the consistent comment is COSO was designed for big companies, and it's the only framework we as auditors have to look to. And so we really need a framework that fits small companies. And I think we thought that's what was going to be coming out of your work that's going to be done in October.

So my question is if that isn't what's coming out, is COSO -- if we were to recommend that we need a right sized framework for internal controls that really does fit smaller companies, is COSO the organization that could do that? Or are you telling us you tried to, you looked at it, and you just don't think you're the organization that could or would be providing that?

MR. RITTENBERG: I would say that's a very tough question. In responding to your question, essentially the task that we were given was to apply the COSO internal control framework to smaller businesses. We did not explicitly set out to develop a new framework. What I said in my written comments is that the fundamental principles of control are the same regardless of the size of the organization. I believe that a smaller business should have an effective control environment. I believe a small public business, and COSO believes this as well, ought to have effective oversight by a knowledgeable audit committee. We believe that a small business ought to have effective controls built into their computer system.

So if we look at all of those issues, we do not believe that the statement that is widely used is that COSO was developed just for larger businesses. We believe the principles are fundamental across all businesses. We intend -- and you will tell us if we fail, but we intend that the guidance will show specific ways that smaller businesses can implement effective internal controls. And it is based upon the principles of what we believe is good internal control. And what we want to see is that smaller businesses take those and implement them. All right?

I think some of the other issues that we've addressed today and elsewhere relates to implementation. And from that point of view, and I've said this to my good friend Dan Goelzer, that COSO is certainly willing to sit down with, not only with the

SEC, but with the PCAOB and say -- and look at whether or not there are implications of our guidance that we need to jointly consider. And if indeed the guidance is not sufficient, we need to go back to the drawing board.

MR. WANDER: Drew?

MR. CONNOLLY: This is Drew Connolly. Mr. Rittenberg, thank you as well for being here. Firstly, I would like to associate myself in total with the remarks of my co-committee member Alex Davern. It is impressive to me that a gentleman who is both the CFO of a major company and also sits on the board of organizations representing 2500, not -- admittedly not all of them public, but 2500 productive, producing, manufacturing, or service companies in this economy can state with some degree of certainty that we have perhaps overburdened the economy, the productive use of both capital and labor with what may very well be an unsustainable regulatory and financial accounting framework. And I am deeply, deeply concerned that in your presentation, I'm not sure I ever once heard the word investor. And there are both institutional and retail investors both sitting in this room and presumably deeply concerned about the results of our work.

And, you know, I recall the advice that I've given a number of young people who come to me in my role in Wall Street and asking me how they should complete their education and where they should be positioning themselves. And the short answer that I've tried to give them is that everybody in outside sales is part of overhead. And I don't mean that in any way, shape, or form to be disrespectful to the accountants and the attorneys and the various other service providers to the public company arena or the regulators in the room who will hopefully use our work product rationally.

But it is disturbing when one takes a look at the magnifier and the multiplier effect of these additional costs that a rational businessman, presuming that we agree that these internal controls will lead to additional enhanced deficiencies within the businesses, etc., that we would need to compel those internal controls and we would be opposed to a phased stage-in over, say, three years of those elements of controls because they might slip or we'd be deferring maintenance. So my question I guess is given why -- if we accept that rational businessmen will lack in self interest, and that internal controls will lead to more efficient and, therefore, more profitable businesses, why is it not possible for smaller public companies who are burdened with the cost able to, in your view or COSO's view, stage those internal controls over a deferred period of time?

MR. RITTENBERG: The public evaluation over a deferred period of time; is that --

MR. CONNOLLY: We have not done that as a committee, but I know there's been some discussion of that.

MR. RITTENBERG: But I wanted to make sure I understand your question. From our point of view, you are correct in that effective internal control is an investment in a company, and it is an investment that should allow a company to grow. And I do believe -- and again, I don't have empirical evidence with me today -- that there are a number of small businesses that aspire to be large businesses that have very charismatic CFOs, CEOs that grow and grow and never make it to that next stage because they have not invested in the fundamental controls to allow that organization to grow. And I think we need to be aware that there are instances like that as well. And so that effective internal control can and should be good business.

MR. JENSEN: I'm Mark Jensen. I'm actually an auditor by background; therefore, I'm overhead, which is actually one of the nicer things I've been called in the course of being an auditor. And I only say that because I just want you to know the position I'm asking the question from. Not exactly under the COSO organization's responsibility, but I'm curious about just your view, whether COSO has a view or your own personal view, about auditor involvement. A lot of the testimony that we've received seems to point the finger at the audit firms as being kind of the culprit in all of this driving the costs up, so on and so forth. And I'm curious from your point of view, is auditor involvement in 404 critical to its being successful in our economy?

MR. RITTENBERG: Let me just give you a personal view on this one.

MR. JENSEN: That's fine.

MR. RITTENBERG: Because it is not something that COSO has examined.

MR. JENSEN: Right.

MR. RITTENBERG: Having studied the profession for well over 30 years and been involved in the profession, my personal view is what you saw last year of auditors doing what they had done best for a long period of time, which is to focus on detailed transactions and detailed testing, rather than zeroing in on what were the major risks to the organization. I think that they are wary of litigation, they are wary of -- some fear being criticized by the PCAOB and the inspection process. And I think the PCAOB has, in a sense, responded to that. I think they have, in fact, learned from that process, and there should be greater efficiency.

From a COSO point of view, if we go back to the Treadway Commission, they recommended public reporting on internal control by management, but they did not recommend in that document that it be attested to by the outside auditor or the external auditor. And we have not reexamined that particular opinion because the law mandated that it be publicly examined by the external auditor.

MR. WANDER: Any further questions or comments? Yes, Janet.

MS. DOLAN: I don't want to be redundant, but your last comment is what all of us are trying to get to, which is if we don't assume that all small companies are trying to avoid internal controls but we do assume they are looking for some guidance on what are the most critical ones that really make a difference, and then are we doing a good job at managing those controls, that's what we're all trying to get to. But nobody seems to be able to help us get there. That's what I'm trying to get at, which is, is COSO an institution that can help us get there by saying, "We will help identify what are the most critical internal controls," or help us get away from -- there's one size fits all that's being applied to everybody regardless of the size. So that's what I'm trying to get at. Assuming that we all want to get to the right end goal, which is to provide good internal controls, how do we get there?

MR. RITTENBERG: Let me respond more directly. I think the answer is yes. I do think that in my role as chair of COSO, one of the first things that I recommended is that we do some strategic planning as how the nature of COSO might or should change to answer those questions. And we have been deferred a little bit because we have focused on this project, but I believe we need to address that. And it may require some changes in COSO. COSO may become broader, COSO may become a more permanent organization, and it may differ in the way it has been in the last few years. It is an organization that is dedicated to those fundamental objectives. But I am open to change, and, in fact, I am in a position, an advocate for change within the COSO environment.

But I think your question gets at a more fundamental one issue for COSO, the answer better be yes, or we shouldn't be in the business. And we believe we should be.

MR. WANDER: Larry, just picking up on what Mark's question was, one of the items that our 404 subcommittee has been discussing and hasn't come to any formal conclusion at all is do we need auditor involvement at least for smaller public companies. And the process, or as the certifications under 302 and 906 and maybe a stronger certification or management reports as COSO originally suggested good enough. So I would just encourage you and COSO to do a little more thinking on that because you may want to respond to a recommendation that we make on that along those lines.

MR. RITTENBERG: We will do so. Thank you.

MR. JENSEN: Could I ask one more question? Just really brief, could you tell us a little bit -- tell the committee a little bit about COSO, how it's organized, how it's funded, how many people you have working there, what your mandate is, how you established standards?

MR. RITTENBERG: Sure. It's a short question that belies a short answer. COSO, when we were founded, was based upon significant contributions by the five organizations that --

MR. JENSEN: And who were they?

MR. RITTENBERG: The American Accounting Association, the AICPA, the FEI, the IIA --Institute of Internal Auditors -- and the IMA. That led to a full staff and significant amount of funds related to the research that supported the National Commission of Fraudulent Financial Reporting. That led to the Internal Control Integrated Framework in which COSO did not feel that within itself, it had a permanent staff to essentially develop that. At that point in time, they issued requests for proposals and engaged the firm of Coopers and Lybrand to help develop the Internal Control Integrated Framework. So COSO as it stood then, and as it stands now, has five board members plus the chair. Each of the board members come from one of the five sponsoring organizations.

We have been funded essentially through the sales of our products over a period of time. I think one of the things in my own personal agenda is that to some extent, and you will see it in my written comments, COSO has been almost a virtual organization over the past few years. It has taken on very large projects. I think there's a perception that all of our projects are done with Pricewaterhousecoopers, or Coopers and Lybrand before that. I came on board as a board member when we did the enterprise risk management project, and we did solicit proposals from a number of companies ranging in the risk area from places like Towers Perrin to other Big Four firms such as Ernst & Young who all proposed. And at that point in time, we felt that PWC had the best proposal.

For each of these projects we have, in fact, engaged a very active task force, we usually ask the task force to be chaired by other than myself. And Debbie Lambert is chairing the current task force related to guidance for smaller businesses. We've tried to populate the task force with people that understand the particular issues. But we do not have an office or a permanent staff, and I think if we are going to have a significant role, in not only supporting research, but providing more guidance in these areas, that we're likely going to have to change. And we'd be open to suggestions that you have there.

MR. JENSEN: We -- just speaking for myself, I guess, and some of the recommendations I've made to our subcommittee, it seems to me that if COSO is going to become -- or is, in fact, the de facto standard, that there should be a formal organization and a formal exposure process. The public should be allowed to comment and things of that nature, because otherwise you've got -- basically you can come up with a standard without any real infrastructure for anybody to look to.

MR. RITTENBERG: I think that's certainly one of the areas I have on my agenda as we look into strategic planning, and I think your insight will be helpful to us.

MR. WANDER: Okay. We're going to move on. Larry, thank you so much --

MR. RITTENBERG: Thank you.

MR. WANDER: -- for your sage advice. And we will look forward to reading your materials and reading the COSO report when it does come out. And I will get you E-mail addresses of all our committee so that we can receive copies of the report when it does come out.

MR. RITTENBERG: Thank you. I'll leave these right here so you can distribute at your leisure. Thank you.

MR. WANDER: What we would like to do now before we adjourn, which is at 1:30, is have reports from our four subcommittees as to the status today. And as Jim stated early in the meeting this morning, by the time of our next meeting in October in Washington DC, we would hope that there will be concrete recommendations from each of the subcommittees to the full Committee so that those can be aired, debated, discussed, and, in effect, finalized in the near future after that meeting so that we can begin preparation of our actual report and recommendations.

Before we go into the reports of the subcommittees, let me make two announcements. One is, and I think Larry mentioned this, that the GAO is doing a study for the Senate on Sarbanes-Oxley and including the application of Section 404. And I gather a number of our members of our Advisory Committee had been interviewed by the GAO, and I have had contact with one of the team leaders from the GAO. And while they can't share information with us, we're fairly transparent with all of the information we have on our web page, we do hope to coordinate some of our activities with them and so that at least we know what each other's recommendations are eventually going to be. We should be coming out with our reports around the same time. And perhaps if there's some disagreements, we could air those and understand them before the final reports are out.

The second is we are trying to schedule a half a day of further hearings in New York City prior to our October meeting. They have not been finalized, a date hasn't been finalized. We don't intend to have the full Committee in personal attendance, although we will have some sort of hook-ups so that people can participate. And the primary source of presenters at that time will be small cap managers, and again, to try and focus on what it is that they are looking for, what it is they need. And we'll let you know about that.

And now I'd like to move on to a report of our subcommittees, and Capital Formation is the first one on the agenda. And I saw Dave Coolidge is in Australia, and I saw Richie leave, so who's giving that report?

MR. CONNOLLY: We've got a deep bench, Mr. Chairman. We've come around the horn, as you know, and largely through the efforts of the two co-chairmen of this Committee. I wasn't actually kidding; we do have a very deep bench with a pretty broad representation of interests and capabilities. So I think that although we are struggling, and I give Mr. Schlein a lot of credit to say that, my God, there may be something here that we just don't have, we're very open to having that displayed or discovered. Because I think that our efforts focus very strongly on what it is that's currently a bar to additional capital formation or where it is within the securities regulations, Sarbanes-Oxley, and others that were they potentially examined for change, would assist in the capital formation process.

We're also very mindful that the document that finally emerges will be lengthy and tome like, so we're attempting to bring it down. I think Richie, as scrivener, has done an inordinately good job of getting us an outline, and I'm hopeful that we can go from there. The good news is that, as I said earlier, number two is their number one. We do have private placement broker-dealers and finders as a key element that we know is currently perking along at NASAA, National Association of North American Securities Administrators, and hopefully will meet less resistance within the Division of Market Regulation from the SEC than it has heretofore.

But our number one recommendation because it goes directly toward how sales are affected, we would like to believe that, you know, you cannot hold your light under a bushel basket, and if we do not do something about general solicitation and allowing investors to be aware, it's going to be difficult for the rest of these capital formation principles to be in place. So our number one recommendation, and I'm just going to be very belief about all these -- I know you don't believe that, but I'm going to try.

MR. WANDER: Why do you think we don't believe it?

MR. CONNOLLY: The number one recommendation, and I feel like David Letterman on this, number one, end prohibition against general solicitation. And there's some verbiage behind that. Number two, private placement broker-dealers, we're very convinced that that is where the rubber meets the road in terms of microcap and small public companies being able to be matched up with capital. Private placements, which is clearly a -- which are often precursors to future public offerings, we have a series of recommendations, A through F there. Rule 701, which is perhaps a bit arcane but has popped up and been problematic most recently in the issues of the public offering at Google, and it goes toward option ownership by employees and insiders and it's going to become self-explanatory.

Number five, there are eight recommendations within the overall recommendation having to do with trading markets. Number six, PIPE relief. Private investments in public equities are often the de facto IPOs of microcap companies, and we're looking to enhance both their applicability and some of the reporting issues so they are perhaps a more transparent source of capital. Number seven, we are mindful of the going private obligations that are currently part of the market place and would like to figure out how to make that perhaps a little simpler. Number eight, we are committed, as are you, Mr. Chairman, I'm sure, from your prior remarks, to providing research both within the framework of how to have conflict free research provided, mindful of the prior abuses, and we will recommend additionally that soft dollar compensation for research be enabled or continue -- enabled and continued, and that we will be supporting company sponsored research.

And then finally, sir, although we are recognizing another subcommittee may choose to take this on, at which point we'll be glad to pass, the discussion of regulation and the potential to, in fact, collapse S-B into S-K while maintaining the benefits of S-B for microcap dollars.

MR. Wander: Thanks, Drew. We'll move on.

MR. LAPORTE: Mr. Chairman, am I to understand from Mr. Connolly's remarks that he wanted this appended to the official transcript of the proceedings? Or is it -- are you just giving a summary?

MR. CONNOLLY: Mr. Laporte, I think it would be helpful if, in fact, we're going to be looking for additional input and also for the Commission staff to be aware that this is where we're headed, yes, we'd like to submit that.

MR. LAPORTE: So this will be a -- for the record of these proceedings, this list of -- like you talked about the eight recommendations, but you didn't describe them.

MR. WANDER: I think -- why don't you -- if you wouldn't mind, Drew, let Jim and I discuss that.

MR. CONNOLLY: Yes, sir. The working papers, sure, we'll let the Chairman decide.

MR. WANDER: Okay. All right. Leroy.

MR. DENNIS: Thank you. Our group has spent -- we spent a lot of time these last two days discussing the responses to the questions that we received that were posted on the SEC's website, and also what I call the tone of the testimony that we received here, although a lot of it didn't really relate except for the last -- today on the accounting side. But we did gather a lot on the tone of what was made. We also spent some time going through the original agenda items that were set and kind of going back to day one making sure that we think we're covering everything that was originally addressed or that we have decided to not address those. And so we did that over the last couple days. I would say our major thoughts are getting very close to final recommendations, and over the next three weeks, we will put those into draft form so that we have those for our October meeting.

The major thoughts are around extension of dates for new standards related to microcap companies. We've talked a lot about the auditor client relationship, we've interviewed the PCAOB; in that, we've interviewed the AICPA. And I think for the most part, we believe the guidance from the PCAOB is working, we'll probably make recommendations that the PCAOB monitor those over the next few months as we go through the filing season, and if additional guidance is needed, that that be issued.

Regarding independence of auditors and the effect that that has on some of the conservative nature we heard, we're heading down the road of some sort of de minimis provisions that allow some sort of judgment be made so we don't end up with well intended but very expensive and maybe inappropriate effects from some of the independence rules. Specifically if we have prohibited services being done by some partner located overseas, does that really impact the independence of a firm here in the U.S.? We talked a little bit this last time about the different regulatory bodies that are out there, the FDIC, and I think the FDIC provides a framework for us because they do have an ability to, in some cases, to step in and be the filing regulator for the SEC on certain banks. And so that may provide some frameworks for how we could expand that to other areas and if there's something there.

Finally in the standard setting process, we are -- we will make a statement that we do not believe political issues should be entered into at all in the standard setting process, that accounting should be accounting, but that simplicity be considered. And we spent quite a bit of time trying to define what simplicity was. We'll probably mirror that with the SEC's paper on accounting standards and come up with some recommendations on how we would view simplicity and how that would be considered. And then finally, I got two or three other items that we need to now think about given the testimony this morning, and so we will -- I will have a conversation with Roger sometime this next week and get together with our group and decide on how to go. But we do plan on having draft recommendations for you by our October meeting.

MR. WANDER: Okay. Corporate -- yes.

MR. SCHLEIN: Are we allowed to ask him questions?

MR. WANDER: I was going to wait to get to the end, if that's all right, Ted.

MR. SCHLEIN: That's fine.

MR. WANDER: Corporate Governance and Disclosure.

MR. BOCHNER: Thanks, Herb. We too have learned a lot over the last two days, both from the Forum and some of the terrific testimony we've heard, and so we've got more to think about. But let me give you a sense of some of the issues that we've been coalescing around for the last six months or so. So I think we're heading towards looking at definitive recommendations in these areas. I think there's a couple more things that are likely going to be strongly considered and perhaps creep onto the list. And the first, I'm pleased to say, is something that this Committee has already recommended and hopefully will be -- and will be considered by the Commission Wednesday and hopefully approved, which is to not phase in the beyond the 75 and 40 days for 10-Ks and 10-Qs, the accelerated reporting. And hopefully we'll get good news on that tomorrow.

We've also been looking at whether the benefits of incorporation by reference, both forward looking incorporation by reference and perhaps even S-3 availability also were widely available or that, you know, the cost savings of being able to incorporate information that's already out there in filings ought to be afforded smaller companies who actually need the cost savings more. And whether access to documents on the Internet, EDGAR is now wide spread enough that we can feel comfortable extending the cost savings, so we've given a lot of thought to that. A related issue is considering whether to recommend to the Commission that they accelerate their thinking on the access equals delivery model that perhaps we don't need to produce all these proxy statements, annual reports in paper copy for everybody. Is there a more rational way that that can be done where those who truly have Internet access don't also have to get paper copies? Maybe, it's time for that default mechanism to apply with the appropriate safeguards for those who still need and want paper copies of those documents.

We have, Drew, looked at -- taken a hard look at S-B, so we do have that in our list. We are looking at raising the threshold, we're looking at somewhere around the microcap definition, so that would be from 25 million to 100 million. We're looking at also whether it would be helpful to eliminate the duplication in regulation and perhaps just have a more simplistic formulation for that relief, and then add to that any additional relief that this Committee proposes such as in the 404 area for microcap companies. SAB 99, Bill Hambrecht, who was before us, also had this materiality issue that Ralph, again, reiterated today, and I've personally seen it in practice, just the frustration between clients and their auditors in figuring out how to deal with materiality issues. So we've got some thoughts there.

The EDGAR system, this -- it's hard to get this one fully baked, but we certainly are hearing a lot about inefficiencies and costs associated with the EDGAR system, and the question gets asked, well, why is it that we can't file in -- you know, via e-mail in Word or PDF or some other format? You know, we'll -- can technology help reduce costs associated with the EDGAR system? So we're likely put forward a recommendation along those lines. Our subcommittee strongly supports the loan prohibition, although consistent with recommendations that are going to be coming from the ABA and also made by the Forum, we think there is a lot of uncertainty surrounding cashless exercises, indemnity advances, and I might even put relocation loans there. And I think clarification would be helpful to the issuer of communities.

There's a few other things that I would say have been sort of floating around the list, but I guess we are -- it's not clear we're going to make recommendations in these areas. But we certainly considered director independence, we certainly considered the 8-K rules to the extent those are burdensome. I think we are going to take a renewed and hard look at the 500 option holder issue that both the ABA and the Small Business Forum will take a look at, and I'm encouraged by those suggestions, and I think we're going to take a renewed hard look at that.

And I guess the last area is just '34 Act disclosure, and I think that -- and we can't really tell if '34 Act disclosure generally beyond 404 is fine for smaller public companies or whether 404 has so overshadowed the debate that nobody really wants to talk about other '34 Act issues. But we have surprisingly not gotten a lot of feedback and comment that there's something broken with respect to other aspects of '34 Act disclosure. But we are, I mean that is on our agenda, and we are open to those kind of comments.

MR. WANDER: One of the reasons I wanted to get through all the reports is because as you can see, there is some overlap. And then we can sort of divide that up. The last report is from Janet on internal control over financial reporting.

MS. DOLAN: Thank you, Mr. Chairman. Unlike perhaps some of the other committees, our committee, because of the nature of our assignment, we are not looking at a laundry list of diverse recommendations, but rather we are looking at -- and I would say we are quite close -- on developing a framework and recommendations for how to apply 404 for all companies within our size recommendation, but a framework that seriously acknowledges and takes into consideration and recognizes the vast differences that there are between companies within our size recommendation. It is premature at this point to preview what that framework will be because we are still not only assessing the ramifications of it, but we are also taking into consideration implementation considerations. But I will say that it's quite clear from some of the questions that all of us have been asking today and yesterday that you could see what some of the elements of that framework, or you can probably conclude what some of the elements of that framework, may be.

I do want to assure the whole Committee, though, that we are close and that we will be ready to share our framework and recommendations in the October meeting, and that we very much are looking forward to the whole Committee giving us their input and engagement. I can say that in Chicago, I think we identified a wide range of options that we were considering, and I can tell you that we have taken a number of those off the table. And I can tell you that, as Jim asked us to do and acknowledged that it is time to do, we are clearly converging around one framework. I can also say that our goal is to strike that right balance between having and imposing and expecting a reasonable level of burden on small companies but weighing that against what level of oversight for internal controls do we think is necessary to provide at least a reasonable level of confidence for investors based on the size of the company in which they're investing.

As Mr. Federman said, I think, so eloquently yesterday when he was here testifying, our committee feels that our job is to ensure that in the 404 fishing net, the holes are not so large that we fail to maintain the market's confidence, but the holes are not so small that we compromise the competitiveness of our capital markets. So this right sizing of 404 will be our goal to strike that very delicate balance. And we think it is challenging, but I think I can speak on behalf of all the members of our committee, we do think it's doable. We think that's our charter, and that's what we will be delivering to you in October.

I also would say that we have a special category, what we call special needs, and that is other certain categories of companies because they are either coming public or they are choosing to no longer be public or have some other very unique characteristics. Should we give special consideration for them, and we will address their needs and make recommendations in those areas as well.

MR. WANDER: Thank you. And now we're open to questions. Ted, I'll let you start off.

MR. SCHLEIN: Leroy, my question is really simple, as to whether you guys are exploring the issue of who can do attestation, whether it -- I don't know if this would be your purview or not, but it sort of is something that Larry was talking about in terms of costs. And Mark actually followed up on, of should we allow attestation be done by certified consultants to create competition in the market place to help drive down costs versus are we in a monopolistic scenario where the very people that are telling you you need to do all these tests and controls are also the people that get to bill you for verifying that you do all those testing and controls, and therefore, certifying you for attestation. I'm just curious as to whether that's an area that you've been debating and think recommendations should be changed or not, and how that then pertains to your very first point around the potentially antagonistic nature between the auditing firms and the companies themselves?

MR. DENNIS: We have not addressed -- I think it related mostly to the attestation of 404 and not -- and I assume not the attestation of the financial statements. So from that standpoint, it's not really part of our committee's agenda to address the auditor involvement in the 404 side of things. I guess I would defer to my esteemed colleague next to me.

MR. SCHLEIN: Then the question is on the floor to anybody.

MS. DOLAN: Well, I would say one of the benefits we're going to get when do make, I think, all of us make our recommendations to the whole Committee, we get the benefit of input, because I don't think we have been looking at is, for all companies, auditor attestation necessary vis-a-vis management attestation. And we haven't looked at the concept of looking at some other third parties who might provide a level of assurance that would be adequate or even meet the needs of the investor. But I will say we have, and it's been certainly a topic of public testimony for us, this question of limited resources, whether you call it a monopoly or just plain limited resources, strain on resources and what that's doing to the cost. So we will certainly take your suggestion to heart and raise it in our committee.

MR. WANDER: Other questions? Mark?

MR. JENSEN: First of all, I think we should take that very seriously. I think it's something that needs to be addressed and discussed in a very open fashion. Leroy, one issue that's been important, I think, here especially as it relates to companies that are backed by venture capital firms or other private equity firms, it's in the area of independence, I think there needs to be some clarity in the up and over independence rules. I think we're going to, it continues to cause issues in the venture capital history especially where you've got a situation where an independence limiting service provider, that one company can prevent you from being an auditor in another company, and a lot of that information isn't available. It's very cumbersome and very difficult. I'll be happy to fill in the blanks if you're not familiar with those rules, but I think that I'd like for you to take a look at that and see if there isn't something we can recommend in that regard.

And I also think the gentleman from Crowe Chizek yesterday was talking about a recommendation around being able to apply AICPA independence rules prior to a company being public and not having the three-year look back for them being independent at all, under SEC rules for all three years. And I think it would be helpful to have those areas explored.

MR. DENNIS: We have discussed the latter, Mark, we haven't discussed what you mentioned earlier. So if you want to give me a call later this week, or John, we'd be glad to float those around our committee.

MR. JENSEN: There's a tremendous misunderstanding out there of what those rules are, and the firms are applying it differently and it's causing some confusion.

MR. WANDER: Debbie?

MS. LAMBERT: It's a question to corporate governances. It has to do with director independence, and you alluded to that just briefly as one of the topics you had at least discussed. I'd like to specifically know if you're talking at all about the group of probably microcap companies, for the most part, that aren't subject to the exchange rules, and, thus, if I understand it, don't have a requirement for independent directors at this point in time because the independent director requirement is driven by the exchange rules, what your thoughts are as a group on that at this point.

MR. BOCHNER: That's right. We've really confined our discussions to the independence standards that were developed by the SEC in the audit committee area coming out of the SOX statute. And the SRO rules you know NASDAQ and the New York Stock Exchange weighing in on independence and doing so by enforcing standards. So we have not delved into the area, and I'm interested certainly in your thoughts on this and others, but should somehow the SEC impose further independent standards on companies that aren't subject to those other requirements.

MS. LAMBERT: I think there's an overlap that we probably ought to have the internal control sub group and your sub group meet. You know, I think we've been coming at that from a control angle, I mean, probably it's something we ought to be talking about together.

MR. WANDER: And if you don't mind, Debbie, I'll sort of elaborate on that a little bit. If there's relief provided under 404 for whatever category of companies, part of that relief would be premised upon the fact that they do have an independent audit committee, do have a majority of independent directors, do have a whistleblower system, for example, things that actually Larry mentioned, the total fabric of the COSO requirement. Well, if you're on the Pink Sheets, you don't have any of those requirements. And so maybe the answer is without -- the answer actually, as Steve and I discussed this earlier, was, you know, maybe you won't condition any relief from 404 unless the company voluntarily complies with those sorts of requirements, which I think almost everybody who has commented to us has said that they are very beneficial to the market place. So -- and they're not applicable to, at least to the OTC, the OTBB, and to the Pink Sheets. Is that a fair --

MS. LAMBERT: Yup. That was great.

MR. JENSEN: I don't know which committee this belongs to. I don't want to follow up on what I said at the end about COSO. I do think there's some recommendations out of the group that are very relative to how COSO is organized, funded. And that whole standard setting body is something we could take a look at and made recommendations. It is a virtual organization. I think it's almost an untenable situation in my mind, so I don't know that the 404 subcommittee should have it-- but maybe Leroy's group could take that.

MR. DENNIS. It's your call.

MR. WANDER: Well, first, I actually discussed that with Larry a couple of weeks ago, and I'm sure that he's going to put that on his agenda when he gets to the point where he wants to do his strategic thinking. But it wouldn't hurt. And I suspect, Leroy, you know, a paragraph or two to actually strengthen the COSO framework and make it more transparent, which is the word of the day, I guess. Everybody wants to be transparent.

MR. CONNOLLY: Mr. Chairman?

MR. WANDER: Drew.

MR. CONNOLLY: Just two quick things. I note that, with the exception of Mr. Rittenberg this morning, we did not get any -- and Mr. Turner yesterday, we did not get any written submissions of the remarks of our witnesses. And my request would be that perhaps we could contact them and ask them to submit, and also if we're going to have an another public hearing, that there be written remarks submitted for the record if that's possible. That's number one.

Number two, with the hope that this sustains and makes it through the final vetting and edit process, going to our, one of our top five recommendations on trading markets, I just wanted to make it fairly clear that from a transparent point of view, that we have two sub-items that may very well cause some discomfort on the part of the NASD. And it would be helpful for us to make them, perhaps, early awareness of that discomfort of that to be included. We're basically going to recommend that rule 15c2-11, information which is gathered by the NASD on every publicly traded filing and submission be made publicly available via the internet. That has been something they have been reluctant to do for many, many years, and it does, in our view, compromise the publicly available information that people need to use to make judgments on investments.

Also we're going to look to hopefully require public disclosure of monthly short interest statistics on the Bulletin Board and conceivably the Pink Sheets, as Mr. Coulson of the pink sheets had indicated he's capable and willing to do. This would tie in and create a harmonic convergence between what is currently required on the major exchanges and the national market system so that the total short interest reporting is available and a market place statistic and, in our view, would, in large measure, confine the potentiality of naked short selling to a defined number. If you're disclosing total short interest and that is capable of being collected from the NASD member firms, we're making another data point, which is now a dark corner of the market place, light.

MR. WANDER: Yes.

MR. VEIHMEYER: I just have one question, I guess, Janet, for you and your subcommittee. If you assume, maybe, that there will be some relief provided in terms of effective date deferral for certain size of companies with respect to 404, has the subcommittee given any thought in terms of the timing of any more permanent recommendations around 404 implementation as to whether it would make sense to get some input from year two implementations before making a more permanent set of recommendations on 404 going forward?

I'm just -- you know, as you sit here the last couple days and listen to a lot of the commentary, it seems to me that there's a lot of conjecturing around what this will look like on a permanent basis and what we will experience in year two. And if, in fact, we get some deferral of the timing of implementation, is that -- have you thought through whether that gives some opportunity to evaluate year two experience before finalizing any recommendations?

MS. DOLAN: We have thought about phase-in of some of our recommendations and how much time it might take to do some preliminary things that might be necessary for those. We have not specifically said well, maybe it's all going to be okay, let's just wait another year and see. I think because cost is one factor, but there also is the consideration of, is this a good use of time and other activities. In other words, is it really value added enough for the layers for the companies of all sizes. So we have looked at timing, but timing in light of if we were to recommend X or Y or Z, how much time would it take and what would have to be done first before it could fully be implemented.

MR. VEIHMEYER: That's really -- I was -- that's kind of exactly what I was referring to, not so much on the cost side, per se, but more as we get into year two from the companies' perspectives, whether there is a clear view around value added and other benefits as you come into a year two implementation, my comments are much more focused on that and learnings from that as opposed to let's just see if the costs go down ten percent or 30 percent. That's not really what I was referring to.

MR. WANDER: Gerry, the questionnaires, did you announce that they -- the answers to the questionnaires, we got, what, about 260? Is that right?

MR. LAPORTE: 263, 264, something like that.

MR. WANDER: Are they now on the web page?

MR. LAPORTE: They are not available on the web page, but we did distribute the answers to all the Committee members last week. It's a 500-page document.

MR. WANDER: Is it going to go on the web page? Do you know?

MR. LAPORTE: We haven't decided that. We need to make it available in the public reference room by the Commission, and we will do that, whether we can discuss that, whether we should post that on the web page or not.

MR. WANDER: All right. I have now read them all. I'd like everybody else to go through that torture. Actually, I thought a lot of them were very astute and very thoughtful.

MR. LAPORTE: We have -- I don't know if we posted them already, but the ones that were from organizations that clearly had no expectation of privacy, I think we're going to definitely post those. But there's a question on some of the others, we didn't -- you know, people faxed them in, and we had told people to keep their identity private, so we have to sort out those types of things. We will probably redact the names of some of those.

MR. WANDER: If anybody has any strong thoughts on it, either let us know now or in the near future on what to do with the vast bulk of comments.

MR. CONNOLLY: Well, actually, if -- Gerry, if they've been identified to the Commission when they were submitted and the Commission has -- or has granted some degree of confidentiality, do we need to at that point -- I mean, in terms of having them made publicly available, perhaps the removal of the -- in other words, what I'm saying is we've received the comments, they need to be made available. Can they be made available without linking source?

MR. LAPORTE: That's what we would do.

MR. WANDER: Yeah, that's what we would do, and that's what we recommended. And in fact, the list that we all got, we got a number but we don't know who the number really refers to. Except, did you -- certain people you can pick out all the way through, particularly the short sellers. We must have had seven or eight people who were very vehement about the short selling on every question.

All right. We're a little bit ahead of schedule, but that's no reason not to adjourn unless anybody has any other -- Alex?

MR. DAVERN: I just have one real quick housekeeping item, it looks like I'm going to have to move my earnings release to come to the next meeting, so I'd just encourage to fix the date for the New York meeting as quickly as possible. I'm sure many others will have earnings release at that time in October also. Or the DC meeting, whichever one is in October.

MR. WANDER: Well, the DC meeting is the 24th.

MR. DAVERN: Is that one day only?

MR. WANDER: Yes.

MR. LAPORTE: This is Gerry Laporte. Herb, I think we had said the 24th and 25th, but we haven't really designated whether that would be a one-day or a two-day meeting. And I think that's what Alex is referring to. We need -- the chairman, co-chairs need to make that decision.

MR. DAVERN: I just wanted to move it to Tuesday, then.

MR. THYEN: We'll decide that this Friday.

MR. DAVERN: That's perfect. Thank you.

MR. WANDER: One day is enough, do you think?

MR. THYEN: Well, I think it's going to depend on how well the recommendations come together and whether they come together in advance of that meeting. If we can come to that meeting with some understanding, then we ought to be able to do it in one day.

MR. SCHEIN: Are you looking for feedback on which of those days?

MR. WANDER: Sure.

MR. SCHEIN: Tuesday.

MR. DAVERN: Tuesday.

MR. JENSEN: Tuesday.

MR. WANDER: The Tuesdays have it.

MR. DENNIS: Herb, I would ask you, I'm not sure -- I don't know whether I agree with Jim, we'll be able to get this done in a day. I think we're going to get a lot of debate this first time through this. So I don't know.

MR. WANDER: Maybe a day and a half. We're very flexible, as you know.

MR. CONNOLLY: And what do you have on the New York meeting?

MR. WANDER: We don't have a date yet because he haven't gotten budgetary authority for it yet. And as soon as we get budgetary authority, we will set the date and hopefully it will be prior to our October meeting on the 24th or 25th.

MR. DAVERN: That's going to be fine.

MR. WANDER: There are a few people, and you'll all be available by phone since our meetings have to be publicly available. And you'll be able to -- we're trying to get a system similar to an earnings call where people -- you know, if you have the right code, you could ask questions.

In any event, I think we should adjourn if there's -- unless there's anything else. I thank the staff as usual for their excellent performance and arrangements and everybody on our Committee.

(Proceedings adjourned.)

CERTIFICATION

I hereby certify the accuracy of this record of the proceedings of the SEC Advisory Committee on Smaller Public Companies.

______________________   11/22/05
Herbert S. Wander   Date
Committee Co-Chair

Index of Written Statements Received

Listed below are the written statements received by the Advisory Committee between its meetings of August 14, 2005 and September 18, 2005 and the dates of receipt.

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Sep. 19, 2005	Kurt M. Swenson, Chairman/CEO, Rock of Ages
Sep. 14, 2005	Robert N. Beury Jr., Chief Legal Officer, Cogent Communications, Inc.
Sep. 13, 2005	Gayle Essary, Managing Director, Investrend Research; CEO, Investrend Communications, Inc.; Executive Director, FIRST Research Consortium; Administrator, Shareholders Research Alliance
Sep. 12, 2005	Gerald V. Niesar, Niesar, Curls Bartling LLP
Sep. 12, 2005	Jean Harris, Greenburg Trauring, LLP, Phoenix, AZ; Stanley Keller, Palmer & Dodge LLP, Boston, MA; A. John Murphy, Wickersham & Murphy, Palo Alto, CA; Ann Yvonne Walker, Wilson Sonsini Goodrich & Rosati, Palo Alto, CA; Gregory C. Yadley, Shumaker, Loop & Kendrick, LLP, Tampa, FL
Sep. 12, 2005	Steven S. Heinrichs, Vice President, General Counsel and Secretary, Neenah Paper, Inc.
Sep. 12, 2005	Gregory C. Yadley, Jean Harris, Stanley Keller, A. John Murphy, and Ann Yvonne Walker
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