

RECORD OF PROCEEDINGS

SECURITIES AND EXCHANGE COMMISSION

ADVISORY COMMITTEE

on

SMALLER PUBLIC COMPANIES

Second Day of Meeting

October 25, 2005

10:00 a.m.

Securities and Exchange Commission

Multi-Purpose Room L006

100 F Street, N.E.

Washington, D.C.

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PROCEEDINGS

The following Members were present in person:

Patrick C. Barry

Stephen E. Bochner

Richard D. Brounstein

Pastora S.J. Cafferty

James A. "Drew" Connolly, III

E. David Coolidge, III

Alex Davern

Joseph "Leroy" Dennis

Janet Dolan

Richard M. Jaffee

Mark Jensen

Richard M. Leisner

Robert E. Robotti

Scott R. Royster

Kurt Schacht

Ted Schlein

James C. Thyen

Herbert S. Wander

The following Members were absent:

C.R. "Rusty" Cloutier

Deborah D. Lambert

John B. Veihmeyer

The following Official Observers were present in person:

Daniel L. Goelzer

Jack E. Herstein

The following Official Observer was absent:

George J. Batavick

The following SEC personnel were present in person:

Anthony G. Barone

Mark W. Green

William A. Hines

Gerald J. Laporte

Kevin M. O'Neill

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MR. WANDER: Before we begin the substantive agenda, a couple of people called in from listening to the webcast and were not absolutely clear on who was who and what the makeup of the various subcommittees are, so I think maybe the appropriate thing to do to begin today's session is to have each of the subcommittee chairs introduce the members of their subcommittee who are here so the people listening and not seeing could try and identify them better.

Since, Dave, you have everybody at your table, why don't you begin?

MR. COOLIDGE: I am Dave Coolidge, chair of the subcommittee on capital formation. Do you want more --

14 MR. WANDER: Introduce --
15 MR. COOLIDGE: I was born in 1943 --
16 (Laughter.)
17 MR. WANDER: We don't want your grammar school.
18 MR. COOLIDGE: Ted, why don't you introduce
19 yourself.
20 MR. SCHLEIN: Ted Schlein, capital formation.
21 MR. LEISNER: Richie Leisner, capital formation.
22 MR. HERSTEIN: Jack Herstein, capital formation.
23 MR. CONNOLLY: Drew Connolly, on capital formation.
24 MR. WANDER: And then we will go over to you,
25 Leroy.

1 MR. DENNIS: Leroy Dennis, accounting standards,
2 and I have with me today the most important committee member,
3 and that is Pat Barry, of our accounting standards committee.
4 That is all we have here today.

5 MR. WANDER: And John Veihmeyer from KPMG, who was
6 here yesterday.

7 MR. DENNIS: That's correct and had to go away today.

8 MR. WANDER: And Steve?

9 MR. BOCHNER: Steve Bochner, the governance and
10 disclosure subcommittee. And we have got Bob Robotti here,
11 Pastora Cafferty, and hopefully Dick Jaffee will join us, and
12 Rusty Cloutier can't be here today.

13 MR. WANDER: Okay. Janet slipped out for a minute

14 but who would like to introduce your committee? Why don't
15 you, Kurt?

16 MR. SCHACHT: Good morning. We are the 404
17 subcommittee. I am Kurt Schacht from CFA Institute.

18 MR. BROUNSTEIN: And I am Rick Brounstein.

19 MR. GOELZER: I am Dan Goelzer from the PCAOB. I am
20 an observer member.

21 MR. JENSEN: I'm Mark Jensen.

22 MR. DAVERN: Alex Davern, with National
23 Instruments.

24 MR. WANDER: And Janet Dolan will be here any
25 minute, and Jim Thyen is my co-chair, and I am Herb Wander,

1 and from the staff, sitting around the table we have Gerry
2 Laporte and Kevin O'Neill, plus there are a number of other
3 staff members here in attendance.

4 And Debbie Lambert is a member of the 404
5 subcommittee and she had some travel problems yesterday, but
6 based on an email, I think she will be here today, so we are
7 looking forward to having her.

8 With those introductory remarks out of the way,
9 what we would like to do today is hear reports from the
10 subcommittees to now tell us after they met privately
11 yesterday afternoon and this morning what their latest
12 thinking is on recommendations, so that the full committee
13 can consider these and hopefully we will probably try at the

14 end of today to schedule an additional meeting sometime
15 before the end of the year, when all of these will be in
16 written form and brought before the committee for discussion
17 and adoption or rejection.

18 So with that as an agenda, are there any other
19 opening remarks by anyone?

20 (No response.)

21 MR. WANDER: And Janet, we will start with you,
22 which is the 404 subcommittee.

23 MS. DOLAN: Good morning, everyone, and to all of
24 those who are tuning in.

25 We made a lot of progress and we have had a very

1 substantive several hours in our subcommittee. We are not at
2 this stage ready to make specific recommendations to the
3 whole committee, but what I will do is tell you where we are,
4 what we are looking toward doing, what we hope to get done,
5 and if we can then we think we are aligned around that
6 recommendation, and if we can't then we'll tell you what we
7 will probably be doing in the alternative.

8 I want to begin by setting a few framework
9 comments. I would reiterate some of what we said yesterday,
10 which is we would reiterate that we think many of the
11 sections of Sarbanes-Oxley and the recommendations that they
12 made for all companies have been and are very effective and
13 should continue for small companies and clearly the

14 whistleblower, clearly the role of independent directors,
15 clearly the 302 certifications.

16 What we have been wrestling with, and I think we
17 have been very clear to this committee and to the public, is
18 that we think we understand and can articulate what some of
19 the fundamental problems were with the implementation of 404
20 as it is currently laid out for small companies.

21 What we are about is trying to create a solution
22 that we think will actually continue to provide what the
23 creators of Sarbanes-Oxley and what the public and what the
24 investors want, and yet will make it a workable framework,
25 404 framework for small companies -- so that is what we are

1 about, and we think what happened, one of the most
2 fundamental things that happened, is that the 404
3 requirement, and there are two separate parts to it,
4 management is required to make their acknowledgement and
5 auditors are required to make their attestation with regard
6 to internal controls.

7 What happened was there is no real framework for
8 what is a good internal control environment for small
9 companies. There is no guide by which they could determine
10 that they in fact had the appropriate internal controls. The
11 only standard that was set was AS-2, which is really an
12 auditing standard, and so that became the de facto standard
13 for everybody.

14 Much of what we have heard in all of the testimony
15 we have taken is that framework is too complex for small
16 companies. It simply isn't the right size for small
17 companies, and so what we are aimed at is can we do
18 something, can we create something that will in fact bring
19 the spirit of 404 to smaller companies but do it in a way
20 that gives them the right size framework by which they can in
21 fact, both management and -- that management can in fact
22 fulfill their requirement with regard to 404. And we are
23 not there yet, but we are getting very close.

24 What we are proposing at this point, what we are
25 trying to shape at this point, and it is preliminary -- I

1 know there were news reports out yesterday -- I want to say
2 this is preliminary. We are in the preliminary stages of our
3 recommendations, but what we are looking at is we are clearly
4 aligned, and as we said yesterday we are clearly aligned that
5 we would not require the auditor attestation for micro caps.
6 We have complete alignment in our committee around that.

7 We would like to maintain the management's
8 obligation to assert to the adequacy of their internal
9 controls. If we can help push forward and see that there is
10 a framework created that they can look at and say this is
11 what I am supposed to have, and if I can have this, then I
12 can make my assertions -- we don't have that now.

13 Our caveat is if we can in the next few weeks, and

14 we will take that on as our goal, to work with COSO or others
15 to see if we could actually make a recommendation about how
16 would we go about creating that framework for micro and small
17 cap companies. If we could create that framework where
18 everyone felt that is a cost effective reasonable framework
19 and standard by which I can hold myself to, we will then
20 recommend that.

21 We will recommend that for micro cap companies it
22 would be the management's obligation to assert their adequacy
23 of their controls based on that framework. We would then
24 look at stepping up as we move up the size of the companies
25 into the smaller companies, bigger than micros but still

1 within our smaller design. They would have the same
2 obligation. Management would assert the adequacy based on
3 the same framework. We are trying to keep this as simple as
4 possible.

5 They would make the same assertion against the same
6 framework, but for that size company, as we indicated
7 yesterday -- we were looking at a role. We would now bring
8 in the auditor's role, but their role would not be to attest,
9 as it is under AS-2, but it would be as part of their
10 auditing function. It would be to issue, to actually review
11 the design and the implementation. And this would require an
12 accounting standard, and we are looking at the viability of
13 that, recognizing -- and as I said, we have an ongoing

14 concern about recommending new standards -- whether that is a
15 good idea or whether we should try to live within the
16 standards we have.

17 So that is why I say we are not ready to make a
18 recommendation because there are obviously issues here around
19 this, but this is the framework that we are looking at now,
20 which is to say having good internal controls is something
21 that investors have told us is important. Having management
22 take a positive role in terms of their assertion is a
23 valuable element of the internal control framework, but only
24 if we can create a cost effective framework by which everyone
25 feels this performs an important value for investors but

1 doesn't create an undue burden on small companies that isn't
2 justified as a cost benefit relationship.

3 We have every intention of seeing if we can develop
4 this recommendation shortly, but if not then we will look at
5 whether it is important or necessary if our only choice then
6 is to exempt, and that is why I laid out we continue to look
7 at is there nothing between exemption and complete compliance
8 with AS-2.

9 We continue to look at some other areas. They are
10 for us further down on our priority list right now, but we do
11 continue to look at some of the special areas, companies that
12 have just gone public, companies that are in distress.

13 We are asked to look at some of these special

14 exceptions, and we do want to reiterate that we think the
15 governance committee should look at if we create exemptions,
16 as we are recommending exempting micro caps and small caps
17 from the full AS-2 attestation requirement, requiring some
18 trade-offs, and for the micro caps, especially the Pink
19 Sheet companies, that would be as a condition of the
20 exemption, they have to take on some governance obligations
21 like independent directors, whistleblower and other
22 requirements that some of us who are listed companies have as
23 a result of our listing standards. That is not within our
24 purview. We are just asking the governance committee to work
25 in tandem with us, that if we start recommending and ultimately

1 do recommend exemptions, we have some trade-offs that we
2 would put in place to keep raising the bar for improved
3 corporate governance and improved confidence of the public in
4 those smaller companies in exchange for the exemption.

5 So that is where we are. I know some of the other
6 committees are far enough along that they are making their
7 recommendations and they are ready for full committee
8 discussion. We certainly are open to committee questions. I
9 just don't want anyone, either in this room or in any sort of
10 media coverage of this, to think that we are ready to make
11 recommendations or are at all final in terms of what we are
12 recommending.

13 First, I would invite any other members of our

14 committee -- I will say we have a strong minority view in our
15 committee that if we can't do this, then exemption is the
16 better course of action, so I want to make that clear.

17 We have made that clear all along. We are
18 struggling with the "let's exempt" or "let's find something
19 in between exemption and AS-2."

20 MR. BROUNSTEIN: This is Rick Brounstein -- just to
21 clarify. The whole exemption for 404 as a backdrop is really
22 what we are talking about just for the micros. We hope to
23 find this interim solution that has a reasonable standard
24 that a company could do without -- you know, that would be
25 cost effective that would allow them to make an assertion

1 beyond just 302.

2 MR. WANDER: Okay. Any other -- thank you very
3 much. I know that you have labored long and hard and you
4 have the most difficult challenge facing, I think, our whole
5 committee, so we all greatly appreciate --

6 MS. DOLAN: Well, we believe you don't have these
7 advisory committees very often, and so it's easy to identify
8 what's broken. It is not so easy to say so how do you fix
9 it. I think from all the questions we have asked all the
10 witnesses, through this process it is very clear. That is
11 what we are trying to do.

12 We are trying to actually do something we all think
13 perhaps should have been done before 404 was ruled out, which

14 is to right size it based on the size of companies, then to
15 set reasonable cost effective standards, and then come along
16 and audit to those standards, but we are where we are, so we
17 are trying to create that guidance for small companies so
18 they know what it is they need to do, and then you can come
19 along as they get bigger and add the auditing of it.

20 MR. WANDER: Any other subcommittee members who
21 would like to comment?

22 Again, thank you so much. Sure, Drew.

23 MR. CONNOLLY: Janet --

24 MR. WANDER: It's Drew Connolly.

25 MR. CONNOLLY: This is Drew Connolly. Thank you

1 very much for both a straightforward articulation of the work
2 product and also the work product. You folks are as a
3 subcommittee certainly putting in the hours. No doubt about
4 it.

5 I am interested in hearing about the dichotomy
6 within the subcommittee between -- where the struggle is.
7 Obviously we are on a calendar where we are trying to get it
8 right, but we are also trying to get it in some form of soft
9 concrete as early as possible.

10 So the struggle within the subcommittee is what?
11 Full exemption across the board and some attempts at -- what
12 is the nature of the struggle?

13 MS. DOLAN: I think the struggle is trying to

14 determine is there a way to expeditiously and realistically
15 create a standard by which small companies know what
16 constitutes adequate internal controls for purposes of
17 management's assertion. As you may or may not know, the COSO
18 report, which we have all heard all through our process,
19 is -- right now the COSO framework is the only framework that
20 anybody looks to, even though I think there's been plenty of
21 concern about whether it really does meet the needs of small
22 companies. Their report is only coming out I believe
23 tomorrow.

24 So it isn't so much a struggle in the committee of
25 is this what we want to do, but there is a struggle in the

1 committee of can we actually do it in a simple,
2 straightforward way that really will work, and our first step
3 is going to be to review that report. Our second step is
4 probably going to have a private -- schedule a meeting with
5 the COSO team and see if with the clarity we are bringing to
6 it in terms of what we are looking for, can they help us get
7 there.

8 MR. CONNOLLY: Just a quick follow-up. Is it
9 true -- I think I heard yesterday that the AICPA is now out
10 with some kind of recommendation on exemptions for micro
11 caps?

12 MS. DOLAN: I have not seen it, but we have heard
13 that.

14 MR. DENNIS: I have seen the draft of the letter,
15 Drew. This is Leroy Dennis. I believe the recommendation
16 says that they support -- and I have to pull this out --
17 something like they support a full 404 for all companies but
18 that if the SEC determines that for micro cap companies that
19 it is not cost beneficial for them, then they would support
20 exemption, so it is a conditional.

21 MR. JENSEN: Drew, let me try to frame this for the
22 committee a little bit.

23 MR. WANDER: It's Mark Jensen.

24 MR. JENSEN: I'm sorry. It's Mark Jensen, and I am
25 sure I'll be very successful in clearing it up.

1 (Laughter.)

2 MR. JENSEN: And when I don't, Alex will correct
3 me.

4 The issue that we have been struggling with, and I
5 think -- frankly I think this is what the implementation of
6 404 has been struggling with -- to kind of reiterate
7 something Janet said -- there's two parts to 404. One is the
8 part that the company does, and the other part is what the
9 auditor does.

10 I will analogize it to a financial statement audit.
11 In a financial statement audit, you have GAAP, and the
12 company understands GAAP and the auditor does, so they apply
13 GAAP to their financial statements, give it to an auditor,

14 and their auditor applies GAAS, Generally Accepted Auditing
15 Standards, to arrive at a report on it. When you get to
16 auditing internal controls, there's no equivalent to GAAP, so
17 when the PCAOB issued AS-2, Auditing Standard 2, they told
18 auditors how to audit internal controls, but it was never
19 really that -- it was never defined "Here's what internal
20 controls look like inside a company for an auditor to audit
21 it," so basically that is why you hear so much angst about
22 auditor involvement, because people believe auditors drove
23 that cost.

24 They did, because we were the de facto -- "we"
25 speaking as a profession -- we were the de facto group that

1 had to go tell companies what to do so that we could audit
2 it. What we are trying to do now is get that clarified and
3 get an equivalent of GAAP for these smaller companies, that
4 there is a standard a company could apply to itself and be
5 confident that it had fulfilled its obligations under that
6 standard without having to be, if you will, held hostage by
7 an audit firm saying this is what you have to do in order for
8 me to be able to audit this thing.

9 So we think that there is a way to do that, working
10 with COSO and some other groups, to find that equivalent --
11 the equivalent of GAAP for internal controls.

12 MR. CONNOLLY: You certainly have brought clarity.

13 MR. WANDER: Leroy.

14 MR. DENNIS: Leroy Dennis. Janet, I certainly
15 appreciate the process that you are going through and I agree
16 with talking to COSO and seeing if there is a middle ground
17 somewhere for small companies.

18 I am -- I guess my auditor in me is coming out
19 somewhat skeptical as to what the conclusion will be, because
20 when I look at internal controls for the micro cap companies,
21 the concerns I have are management's ability to override the
22 system. That goes to things like audit committee and tone at
23 the top and whistleblower and those kind of protections that
24 404 does not necessarily address.

25 I wonder if you guys have talked about those kinds

1 of things in your committee and whether -- I mean does
2 that -- it seems to me that leads me more towards maybe
3 not full exemption but 90 percent exemption with some add-ons
4 to some other pieces of this, and I fully support going to
5 talk to COSO to see if we can come up with something. I just
6 don't know, as Herb said, if the book is this big I doubt it
7 is very light.

8 MS. DOLAN: Yes. That is why I said we really need
9 to work in tandem with the governance committee, because we
10 are certainly looking at the auditor attestation part going
11 away, and that the -- as a requirement -- or as a condition
12 for that going away, we would look at putting more certainty
13 into the mechanisms that appear to help most in small

14 companies, particularly for those that aren't required to do
15 them now, and that is, 302 and whistleblower and the
16 independence of the directors and the independent directors
17 on the audit committee, and perhaps even financial acumen on
18 the audit committee.

19 But that's exactly what we're suggesting. We're
20 really -- what we're trying to work with COSO, and Mark keeps
21 reiterating it so I think we want to keep reiterating. There
22 are two parts to 404, and we're already talking about
23 exempting the auditor attestation part. What we're talking
24 about is on the management side.

25 And I know your reservations are well-founded.

1 That's what we've been struggling with. If we can't get
2 there, we will get to the issue of complete exemption from
3 404. But we're trying to maintain that management part,
4 because we do think it's important. We think it's an
5 important sign of confidence -- that builds confidence in the
6 investor marketplace.

7 MR. DENNIS: The other thing I'd ask your committee
8 to take a look at -- you know, and Mark and I live in the
9 auditor world, so we live in this world of auditor
10 expectation gap between what a financial statement audit does
11 and what it is expected to do in the public markets.

12 I'm a little concerned. I'd just ask that you
12a address

13 this in your communication. When an auditor is involved in
14 just the design, we need to make sure that the expectation is
15 set right in the public's mind so that there isn't an
16 expectation that that's going to find all fraud when that's
17 not what the work is going to do.

18 MR. JENSEN: Leroy, that's clearly -- that's
19 exactly the crux of the whole argument, is -- it really --
20 this time we believe -- and I'm speaking for the committee --
21 that if -- just having PCAOB -- asking the PCAOB to adopt a new
22 standard on -- which would basically be design and
23 implementation, and probably some walk-throughs, but would
24 not -- you would not look to the effectiveness of the
25 controls. There would be none of the detail testing down

1 below that.

2 The reason that COSO needs to be involved is that
3 that has to be well understood, what that's going to look
4 like, before that standard gets adopted, or, you're right,
5 we're going to be right back to where we started from, and
6 that is, the audit firms basically telling people de facto
7 here's how that's going to look.

8 And then basically the public accounting profession
9 is going to be back in the gunsights of all the companies for
10 driving all this cost.

11 So we think that has to be done first, get the cart
12 back behind the horse again, and get an equivalent of GAAP

13 out there for these companies.

14 And you're absolutely right. In a smaller company
15 environment, the biggest reason to exempt them in the micros
16 is, the auditor's not relying on those controls anyway, I
17 mean, because of management override and some of the other
18 issues.

19 MS. DOLAN: And I would say I think it's probably
20 been obvious to everybody on the entire committee, but we are
21 trying to triangulate between some very strong forces.

22 One is this issue of creating a liability, either
23 regulatory or legal liability, and this concern that no
24 matter what you do, you're creating a liability.

25 We also -- we're triangulating against -- another

1 factor was, well, why don't we just exempt everything under
2 404, but we'll just create kind of a more complete and more
3 robust financial statement audit.

4 I mean, you know, we looked at, well, why don't --
5 do you build from the floor up or do you take from the
6 ceiling and take off? I mean, that's kind of what you're
7 doing.

8 And we decided that isn't a good idea because you
9 really want -- you want a very standard definition of what a
10 financial audit is for everybody. You don't want to start
11 creating sort of different kinds -- so we sort of avoided
12 that one.

13 And then the third one is the price-value
14 relationship. I mean, that ultimately is the real question.
15 Can you do this and make it something that's valuable for the
16 marketplace, and yet cost effective for the company?

17 So we're trying to juggle all three of those. And,
18 as I say, if we can't get there, we won't get there, but we
19 think we're getting close enough so that we can at least try
20 to formulate that as a framework that people can really look
21 to.

22 MR. WANDER: Sure, Ted.

23 MR. SCHLEIN: Ted Schlein. Whatever type of
24 certification or attestation you come up with for the auditor
25 side, especially between the \$100 million and \$700 million,

1 trying to stick to that area, are you also considering
2 opening up the ability for a certified consultant to do that
3 certification, to create a market dynamic to help drive costs
4 down, so it's not purely an auditing function.

5 Whatever you end up with, it's kind of going to be
6 a parallel track to always go down as you're continuing to
7 refine what type of certification or attestation you're
8 actually going to require for that group of companies or not.

9 MS. DOLAN: The answer is no, we haven't considered
10 it. It isn't, no, we won't consider it, but that we haven't
11 talked about -- we, first of all, want to -- I hate to use
12 the word -- define the word "it" first, and then we can go on

13 to further issues about who might do that and things like
14 that. So --

15 MR. WANDER: Rick?

16 MR. BROUNSTEIN: Yeah, just to -- this is Rick
17 Brounstein -- just to comment to Ted.

18 It would seem like there's such a interrelationship -
-
19 if we're going to cut back to what you've gleaned from the
20 financial audit, that my first reaction is, it would be very
21 difficult to have someone come in who hasn't been associated
22 with the company otherwise to look at the design and the
23 implementation of those controls in a vacuum.

24 But I don't think we've -- we've not specifically
25 addressed that at this subcommittee.

1 MR. WANDER: Any other questions or comments for
2 Janet or any of the members of the 404 committee? We're all
3 looking forward --

4 MR. JENSEN: Steve Bochner wants to --

5 MR. WANDER: I'm sorry, was there --

6 MR. JENSEN: I was just wondering if Steve
7 wanted to comment about corporate governance and how he feels
8 about this area of microcaps and tightening up on corporate
9 governance down there.

10 MR. BOCHNER: Sure. Steve Bochner. I was going to
11 wait till my presentation, but I'd be happy to.

12 So our subcommittee has been doing some thinking
13 about this also, and we applaud the effort. It sounds like a
14 lot of progress has been made in addressing the cost burdens
15 associated with 404. And we think to the extent that you
16 head towards a solution which eliminates the auditor
17 attestation in some way, shape or form, we do think that it's
18 an appropriate quid pro quo to that to have some sort of
19 increased hygienics, increased protection for investors
20 consistent with our mandate.

21 And so the kinds of things we've been talking about
22 would be imposing on those companies that we would allow to
23 opt out of or escape from the auditor attestation, enhanced
24 disclosure regarding the internal control framework within
25 the company.

1 Today it's really at a material weakness level, and
2 so we would be thinking about just an increased -- increased
3 and much more robust disclosure perhaps in items 307 and 308
4 of S-K, where you'd actually have to perhaps get behind what's
5 currently required and give a much fuller description of the
6 control environment and the issues.

7 So increased disclosure would be one leg of the
8 stool. And then, even for microcap companies that don't have
9 it today, to opt out of the attestation. We would think you
10 would want to apply additional governance requirements, for
11 example, audit committee independence.

12 Secondly, would be audit committee financial
13 expertise so that the investing public that doesn't have the
14 attestation because it costs so much at least can feel like
15 there is an audit committee, they are independent, and there
16 is some financial expertise. I think the CEO-CFO
17 certifications are a good idea, to impose that as well.

18 And then the final element that we've discussed
19 would be whistleblower protection. There would be a report
20 up to the audit committee.

21 I think there are some challenges we're going to
22 have in formulating those, and there's some legal issues
23 there. But we could either -- to the extent the SEC could do
24 this, to impose those requirements on those set of companies
25 that are able to, to not have the auditor attestation.

1 Or a fallback would be require disclosure of those
2 governance items I mentioned as a fallback if we can't impose
3 those governance standards directly -- the SEC can't impose
4 those governance standards directly on companies.

5 But that's a legal issue that we'll be able to
6 resolve along the way.

7 So we -- I think our thinking is very much aligned
8 with yours in that regard, and those are sort of the elements
9 that we've been talking about that would be the quid pro quo
10 for no attestation.

11 MR. WANDER: Any comments back to Steve from Janet,

12 you, or any members of your committee? Do those seem to fit
13 within what you've been looking for?

14 MS. DOLAN: Yes. I mean, that's the usual list
15 that we talk about.

16 MR. WANDER: I think the only new one is this
17 increased disclosure --

18 MS. DOLAN: Increased disclosure, right.

19 MR. WANDER: -- which maybe -- maybe you can weave
20 that into your -- however you come out here somehow.

21 MR. JAFFEE: Herb, a question.

22 MR. WANDER: Yes, Dick.

23 MR. JAFFEE: And I apologize for my --

24 MR. WANDER: Dick Jaffee.

25 MR. JAFFEE: Dick Jaffee, and I apologize for my

1 late arrival, and maybe this has already been asked and
2 discussed.

3 If we didn't have the auditor attestation -- and
4 it's my understanding that there's really two of them - they
4a have to make
5 an opinion on the internal controls and then on the company's
6 appraisal of their own internal controls. So you end up with
7 a financial statement -- three different attestations. Is
8 that correct?

9 MR. BOCHNER: That is, I think.

10 MR. JAFFEE: Okay. So I'm assuming that if we

11 opted out of that, we'd be back to one, as we traditionally
12 used to have.

13 If that were done then, one of the issues that I've
14 heard talked about a lot is, because the auditors had these
15 other two attestations to make, they couldn't help the
16 companies in designing the internal control system because
17 they then would be opining on their own work.

18 If we got rid of these other two attestations,
19 would the auditing firms be freed then to help the companies
20 put internal control systems together and work through this
21 thing? Still wouldn't?

22 MR. DENNIS: This is Leroy, Leroy Dennis. I think
23 they would be available to help under the PCAOB guidance, but
24 I still don't think that the auditor is going to be involved
25 in designing and implementing systems, that it's eventually

1 going to audit financial statements that are created by those
2 systems.

3 So I think we'd fall back to the PCAOB guidance that
4 was issued, which I think -- at least my reaction is working
5 and is getting to a desired result. But I don't think we'll
6 be in a mode where the auditor -- or the management will say
7 to the auditor, design for me an internal control system that
8 I can then implement and you can come in and audit later on.

9 MR. JAFFEE: See, because I --

10 MR. GOELZER: Yes, I would agree. I think even --

11 I'm sorry, Dan Goelzer. I think even without the element of
12 the auditor having to opine on the system or on management's
13 assessment -- because the auditor inherently uses the
14 controls -- relies on the controls as part of the audit, that
15 there would still be limits on the ability of the auditor to
16 create the controls for the company.

17 But, as Leroy suggested, we tried to give a lot
18 more latitude for discussion and back and forth between the
19 auditor and the company in the statements we put out in May.
20 And if this kind of change were made, then possibly that
21 could be revisited and liberalized still further.

22 MR. JAFFEE: Yeah, Dick Jaffee again. It just -- I
23 think the sequence of events, the way this thing was
24 implemented, I know in our own case, we got going before the
25 PCAOB guidance, and so we had to bring in -- somebody asked

1 about getting a consulting firm in to help you.

2 We got outside people, not our auditors, and so
3 they had such a learning curve, and such a costly one, to
4 figure out what our business was and all that, that that's
5 one of the reasons why all the costs blew up on this thing.
6 So --

7 Anyway, it is what it is. I think liberalizing it,
8 if the PCAOB would do it in light of this, if that's what's
9 ultimately accepted, would be very helpful.

10 MR. GOELZER: Dan Goelzer again. If I could just

11 make a quick comment. Building on what Janet said, I think
12 we envision that this proposal would only work if you could
13 have a simple enough framework for management that -- there
14 might still be cases where you'd need consultants, but by and
15 large it would be something that management could do on its
16 own, without having to bring in a lot of high-priced external
17 talent.

18 MR. WANDER: Hoorah. Yes, David?

19 MR. COOLIDGE: Yes. A question on independent
20 directors -- Dave Coolidge, excuse me -- independent
21 directors and independent audit committees for microcap
22 companies, which is -- and my concern there is the ability
23 for those companies to attract the financial experts, the
24 truly independent directors.

25 And this came up earlier in some of our discussions

1 about whether some of the bright line rules that define
2 independence could be relaxed a little bit from a materiality
3 standpoint so that these companies could -- you know, they'd
4 kind of be out of the frying pan into the soup if they get
5 rid of attestation.

6 But then they have to completely rework their
7 boards because everybody is deemed not to be independent
8 because they -- it might be their, you know, consultant or
9 advisor in some other regard. I'd worry about that.

10 MR. BOCHNER: Yeah, Dave, I think that's a good

11 point. We'll -- in formulating our recommendations along
12 these lines, we'll take a look at that. I suppose we could
13 look at whether -- I think the issue is helped along if these
14 microcaps aren't subject to the full majority independence
15 requirement. So you're really focused in on the audit
16 committee. So at least from a numbers point of view, you're
17 better off right away.

18 But to your point, maybe three fully independent,
19 within the meaning of the current SEC rules, with no
20 basically compensation and tolerant independence, which is
21 what the audit committee requirements insist on today, maybe
22 there could be some sort of relief with respect to that
23 category of companies.

24 Or maybe the audit committee composition could be
25 smaller than three. As long as you have independent

1 individuals with perhaps some safe harbor about other
2 compensation that would -- you know, that would allow some
3 flexibility there. But we don't have that thought through
4 yet.

5 MR. BROUNSTEIN: Can I add on to that? One of the
6 pieces we got was -- I don't know if it was an ABA-generated
7 piece, but it was what a group presented that was associated
8 with ABA, and they talked about, for smaller companies, the
9 notion of a strategic investor, and maybe, you know, when you
10 look at the definition of independence, somebody like that

11 that wouldn't -- that, again, big companies and little
12 companies are different, and we need to take a look at the
13 sizes.

14 So I think there's some data out there that the
15 committee can look at when they start to formulate this.

16 MR. WANDER: Drew?

17 MR. CONNOLLY: I'd just like to follow on -- Steve,
18 if I -- this is Drew Connolly. I'd just like to follow on to
19 Dave's issue.

20 And I think the concern I have is not only -- the
21 issue of independence, I guess, will be settled one way or
22 another. My concern is the availability of financial expert
23 directors for microcap companies.

24 All of a sudden we've created this major demand for
25 independent directors, and we've created this major demand

1 for financial experts.

2 I can assure you that a number of the microcap
3 companies I'm familiar with would find it very hard to
4 compensate that director at a level that I think someone
5 who's a financial expert and who would assume directorial
6 liability would expect to be compensated.

7 So there's sort of a concern there as to how to
8 make it work in the real world.

9 MR. BOCHNER: Yeah, I appreciate those comments,
10 Drew, and I think we do have to be realistic about what a

11 microcap pink sheet company can do in attracting directors.

12 I think we're trying to figure out -- we're trying
13 to do a balancing act here and say if we take away the 404
14 attestation and eliminate that protection because the costs
15 are too high, what is the right counter-balance to provide
16 that investor protection?

17 And you could say nothing, just eliminate the 404
18 attestation and go on with life. I think there is some
19 sentiment around the table that says no, we ought to -- you
20 know, there ought to be some sort of quid pro quo, and maybe
21 we need to continue to discuss what that ought to be among
22 those things I mentioned, none of which I think are in stone
23 yet.

24 But I do think -- I do think the elements of it
25 would include some aspects of governance assurance might be

1 better than what exist today for those companies, whatever
2 that is, and some enhanced disclosure that allows a peek
3 behind just the material weaknesses to the actual control
4 environment to provide that enhanced disclosure.

5 So I welcome all your thoughts about where we ought
6 to draw that line and how far we ought to go in the
7 governance area.

8 MR. WANDER: Rick?

9 MR. BROUNSTEIN: Okay, Rick Brounstein. Among many
10 hats I wear one of them is I'm active in an organization

11 called Financial Executives International. I have a document
12 here about FEI. And there are other organizations out there.

13 But I would push back on that and say, you know,
14 there is -- we maintain a registry at the national level for
15 CFOs who are interested in filling those kind of roles, and
16 that registry is actually fairly long and not very often
17 tapped, so -- and there are others out there that I'm aware
18 of, too.

19 So I think when we get into it, I think we may find
20 that there's more of an appetite for people to get involved
21 than you think on the surface.

22 MR. CONNOLLY: Once again, Drew Connolly. Rick,
23 I'm happy to hear that. I was unaware of that registry, and
24 I can assure you that if that registry exists, and there are
25 folks who are prepared to act in a reasonably compensatable

1 way, there are dozens of microcap companies I'm familiar with
2 who will be looking to tap into it.

3 MR. WANDER: I think I was going to comment, Steve,
4 that if your committee -- subcommittee looks at the COSO
5 study that was done on fraudulent financial reporting, the
6 11-year study -- this was before, obviously, 404 -- but they
7 identified the weaknesses that caused the fraudulent
8 financial reporting, or at least seemed to cause them.

9 And you are in sync with them, but you may want to
10 re-look at that just to see if there's anything else they

11 noticed, particularly the ineffectiveness of audit committees
12 and lack of independence, and the fact -- as I recall in that
13 report -- the audit committees hardly met, even, so --

14 I think the landscape has changed with the
15 strengthened governance for all companies. But that might be
16 sort of a good model for you to check against.

17 Leroy?

18 MR. DENNIS: Leroy Dennis. I just want to support
19 Rick also. And I would say, as far as the -- if getting
20 audit committee independence allows the internal control
21 subcommittee to be more aggressive in its recommendations on
22 controls, I would wholeheartedly support that.

23 But I also wanted to ask the internal control
24 committee -- and I thought of this as Dick was talking about
25 the different levels of attestation that are done by the

1 auditor -- have you thought about, for the microcap
2 companies, maybe splitting that baby a little bit and looking
3 at whether or not we'd ask management to opine on design and
4 implementation only, but not the operating effectiveness of a
5 control system in their attestation for the microcap?

6 And is that a way to take maybe a still more
7 complicated framework that may come out of here, but require
8 some kind of involvement of management to assert on its
9 internal control, but maybe not engage outside consultants to
10 test and all of the things that management has to do also in

11 all this.

12 MS. DOLAN: No, we haven't. That's why these full
13 committee meetings are very helpful. So we will certainly
14 take that into consideration.

15 MR. DENNIS: Something that Dick said that I just
16 thought about, and so I would ask you to take a look at that,
17 as to whether we should split that baby a little bit, too, at
18 management's level.

19 MR. SCHLEIN: Ted Schlein here. I just wanted to
20 clarify my consultant comment because I think the -- at least
21 my point of the significance has kind of got lost from Dick
22 and Richard.

23 My point is, the people that are telling you what
24 you need to do being the only people that can tell you that
25 you've done it, creates an unhealthy market dynamic.

1 And all I'm really saying is, create a marketplace
2 for people that are able to at least tell you that you've
3 done it. And if they're not good enough, then they'll go
4 away in the marketplace, and if they're good at doing that,
5 it should effect driving costs down. It's what creates
6 competition for who can attest.

7 Now, of course, if we'd do away with attestation.
8 This is relatively a moot point so I withdraw the suggestion.
9 But to the extent that some level of attestation or
10 certification is necessary, I'm saying open it up to

11 qualified people -- and "qualified" to be defined -- to allow
12 any number of people to be able to say, yes, you have met
13 this level of controls, and we agree.

14 And I think that will have the desired market type
15 effects, which is to drive the costs down, and obviously also
16 to take away maybe some of the antagonism between auditor and
17 company.

18 That's really the basis of my comment.

19 MR. WANDER: Jim?

20 MR. THYEN: Janet, perhaps the internal control
21 committee can share with us what all you discussed on the
22 apparent disproportionate focus on the process and
23 transactional aspect of 404 certification, and how that might
24 be or not be a detriment to preventing and detecting fraud.

25 MS. DOLAN: Well, you might have to repeat the

1 question. I think that I'll answer it as best I can. Then
2 you can tell me if I tell me if I get to really your
3 question.

4 MR. THYEN: Okay, all right.

5 MS. DOLAN: One of the, I think, reasons for
6 eliminating the auditor attestation is that right now the
7 only framework for the auditor attestation is AS-2, which is
8 very transaction-oriented. And so that's the only framework
9 right now.

10 And I think the conclusion is that we've heard a

11 significant amount of testimony that, as implemented for
12 small companies, that just doesn't produce a price-value
13 relationship.

14 So the idea of getting the auditor attestation off,
15 but still focusing on the management assertion is that if we
16 can actually create a -- sort of a best practice for good
17 controls, internal controls, it may alleviate some of that,
18 because it won't necessarily focus so much on the
19 transactional.

20 It may focus on the ones that are most critical to
21 the integrity of the financial statements, which is where it
22 should be.

23 So we're hoping that we'll get there through that.
24 I don't know if that answers your question.

25 MR. THYEN: It does. Thank you.

1 MS. DOLAN: Okay.

2 MR. BARRY: Pat Barry. On, Ted, what you said, I
3 think those firms actually do exist. We're using -- have
4 interviewed several firms as we were looking at 404, and they
5 work with the big accounting firms to understand what their
6 requirements are, and they would help us, not only design the
7 process, but do management testing on those requirements, et
8 cetera.

9 Although they can't attest to it, they can sort of
10 help us all the way through to do management's piece of the

11 404 work, and pretty much make sure we're compliant with what
12 the auditors were going to look for.

13 I'm not sure if that totally gets to your point or
14 not, but there's a fair amount of firms out there that are
15 doing this work. They just can't do the attestation.

16 MR. DAVERN: Maybe I can reconcile the two views
17 here. I think what Ted is saying, Pat, is that you have a
18 different firm that gives you a financial statement audit
19 than gives you 404 audit attestation. Is that correct, Ted?

20 So you would have one firm that would do an audit
21 report on your financials and another firm that would have an
22 attestation on your 404 work.

23 MR. SCHLEIN: That's possible. My point is, make
24 that possible. That may not be what a company chooses to do,
25 for whatever reasons, but if you make that a possibility, I

1 think you'll find new industry segments rise up to the
2 challenge to be able to do that attestation, do it in a valid
3 manner, and as a result, drive costs down.

4 You may stick with your same auditing firm to do
5 both, but I bet the overall costs will have come down because
6 there's competition.

7 MR. DAVERN: And I would agree, and that's been a
8 strong recommendation of the American Electronics Association
9 I've been associated with for over a year now, that we would
10 do that.

11 Having said that, I think that Rick's point is also
12 true, and that certainly if we eliminate the auditor
13 attestation requirement for microcap companies, it becomes a
14 moot point, as you said.

15 And if we're successful in creating a separate new
16 set of auditor attestation related to design and
17 implementation as opposed to attesting to the operating
18 effectiveness of controls, I think it will also significantly
19 reduce the burden.

20 But I think, in general, for 404, which may be
21 beyond our remit, I think it would be a very good competitive
22 step to bring down the costs for all companies, and I think
23 would also help to create more competition in the market for
24 audit services for public companies, in general, which is
25 probably a good public policy end result. Thank you.

1 MR. WANDER: Sure. Dick?

2 MR. JAFFEE: Just one more question. Dick Jaffee.
3 Janet, in your deliberations, you've obviously done a lot of
4 good thinking and a lot of it focused around the cost-benefit
5 relationship of this thing.

6 Did you have any time to think about whether --
7 even putting cost aside, whether or not the way 404 is being
8 implemented in many small companies, that the end result is
9 actually an improvement in internal controls, or whether
10 perhaps it's been somewhat counterproductive, and that a

11 different approach would have a better outcome?

12 MS. DOLAN: Well, I would kind of answer that the
13 same way I answered Jim's question.

14 MR. JAFFEE: Yeah, it's the same question --

15 MS. DOLAN: Our goal is not to help management of
16 small companies implement AS-2, and just not have
17 attestation. We happen to think AS-2 requires too much focus
18 on transactions that probably don't create enough value for
19 small companies.

20 So our goal is to try to say, can we create a
21 standard for good internal controls that really is
22 right-sized to small companies? That's what we're trying to
23 do. So it isn't -- and cost is a factor, but we're trying to
24 actually create an end product that will be useful, or ask
25 that the SEC direct that somebody do it.

1 We're not going to design it. We just want --
2 we're going to advance it far enough that we think this is
3 doable, and we're going to recommend that it be done.

4 MR. WANDER: Rick?

5 MR. BROUNSTEIN: Yeah, Rick Brounstein. Just --
6 maybe it's obvious, but for the most part what we're talking
7 about when we deal with the smallest of the small -- the
8 microcaps -- is -- today the nonaccelerated filers.

9 So we're talking about, for the most part,
10 not absolute, but for the most part -- these are the

11 8,000 companies that have not had to go through 404 yet and
12 have a very different makeup to them. We think there's a lot
13 of reasons why they are different than bigger companies.

14 MR. WANDER: One other area you might consider
15 exploring -- I don't say you should explore it -- and I've
16 gotten half-a-dozen or so or more advertisements from
17 software companies touting their software package, that it
18 will reduce your 404 efforts and costs by significant
19 numbers.

20 And I don't know whether that works. I do
21 recall -- Alex, you'll probably remember this better -- that
22 the NASDAQ recent survey asked company executives whether
23 there was help on the way from the software companies, and,
24 as I recall, the answer was rather negative.

25 MR. DAVERN: Alex Davern. That's correct. The

1 perception was that it would have a minor positive effect on
2 reducing the cost rather than a significant effect. And
3 that's been certainly my personal experience -- I haven't
4 gone down that road -- that software does add some
5 reusability in year two, et cetera.

6 But in terms of automating this process, it's not
7 effective. You have to physically go and check these
8 controls, walk through them and test them with a person.

9 So it's unfortunately not a silver bullet that will
10 make a significant difference, in my opinion. Thank you.

11 MR. SCHLEIN: Ted Schlein. As somebody that's
12 financed a couple of these compliance software companies,
13 just if you're interested, a lot of what Alex said is quite
14 accurate.

15 There's usually two halves to it. There's the
16 documentation of the policy that you want enforced. And
17 every company has got to have a way to document that, print
18 that out, hand it to their auditor, hand it to whoever's
19 doing the attestation, and then there's the enforcement of
20 this policy.

21 The enforcement of the policy is actually the
22 harder portion of this. But there is progress being made on
23 things like separation of duty, making sure separation of
24 duty takes place, and tracking things like those payments,
25 double account payments.

1 So from a financial system standpoint, we are
2 getting better at automating some of those things, but
3 there's a cost to even implementing that. So --

4 MR. THYEN: I know -- this is Jim Thyen. I know at
5 Kimball we did experience, particularly in our electronics
6 segment -- and here we're getting into a little bit higher
7 size. We're above the micro.

8 But the commitment to an integrated operating
9 system standardized worldwide, which brought with it a
10 commitment to prevention and pushing all the decisions up

11 front, not making decisions -- the authorizations on the back
12 end, really putting emphasis on the contracts entered into,
13 the purchase orders, and all those controls up front,
14 definitely lowered our costs and increased our productivity.

15 Now, there is -- and it helped us in 404
16 certification. But there clearly is a size threshold, that
17 you have to be a certain size to be able to pay for the
18 software, offer it, and make all the commitment to training
19 and the whole mindset change.

20 And it's not down in the micro level. It's even
21 not down in the lower levels of what we're defining as a
22 smaller public company.

23 But that is the only way that we found that we
24 could greatly reduce the cost of our certification. And it
25 so happened we did it for better operations, and to be able

1 to better serve our customers. We didn't necessarily drive
2 it totally from internal control, but we embraced that
3 internal control concept in doing it.

4 I'll just offer that for what it's worth.

5 MR. WANDER: Yes. Mark?

6 MR. JENSEN: It's Mark Jensen. To kind of react to
7 all of that, one of the things we've debated a lot in -- or
8 talked about a lot -- and you're going to see how strongly I
9 view this -- is -- we're back to this issue of who's the
10 final word on what is enough and what needs a threshold for

11 management to be comfortable, making the assertions, and
12 basically taking on criminal liability when they do that.

13 And right now the final word on that is really the
14 auditor. And so the question is, is that the appropriate
15 place -- that's what makes the software difficult to develop,
16 because at the end of the day, it's still an auditor who has
17 to say, yeah, I can accept that.

18 And so I think pushing -- and one of the things
19 we're going to be working on over the next couple of weeks, I
20 hope, is, with COSO, to -- is there some role that COSO can
21 play in a more active -- or the SEC or the AICPA or some
22 standard-setting body that can start to put better clarity
23 around what does it look like when we're done.

24 What's the standard that we can hold that everybody
25 can agree to in these smaller companies, that isn't a

1 nebulous standard set by -- well, at this level you're going
2 to be talking about 100 firms with different standards. But,
3 really, is there a standard that we can all work to?

4 And I think if you get there, I think the software
5 products become much more -- you know, they're going to
6 reduce the cost a lot, because they will be a standard that
7 everybody's going to center on.

8 Today that doesn't exist, and I think that's a big
9 hole in our system. Because COSO, as we pointed out in
10 San Francisco, is -- it's basically a virtual organization.

11 It doesn't have an employee. Even the CEO is only part-time.
12 And to my knowledge, they've never been authorized as a
13 standard-setting body. It's been something that was created
14 and kind of endorsed, and doesn't really have any
15 standard-setting authority.

16 MR. SCHLEIN: Didn't we hear from the guy that ran
17 COSO the last time we got together?

18 MR. THYEN: Yes.

19 MR. SCHLEIN: In San Francisco, right?

20 MR. THYEN: Mark, in a way, I agree with what
21 you're saying, and there's that gap that's got to be filled.

22 But when I look at it from my viewpoint, the
23 ultimate arbiter becomes the customer in the market, because
24 if we just keep driving controls with no concern for cost, we
25 can be absolutely perfect and out of business.

1 MR. JENSEN: No, I agree. I agree with that.

2 Yeah, we did hear from the guy at COSO. He's a
3 college professor.

4 MR. SCHLEIN: Right, but my point for bringing it
5 up, if I remember the testimony, or whatever that was, it was
6 basically -- I thought that he was not proposing really any
7 changes to SOX 404, or any easing of it --

8 MR. LEISNER: Your memory is aligned with some
9 other folks.

10 MR. SCHLEIN: So relying on that as the basis for

11 whatever we're going to come up with for our \$700 million and
12 below threshold does not seem to get the relief that I
13 thought you were alluding to, Janet.

14 So that's -- maybe I missed something there, but --

15 MS. DOLAN: Well, I think that's why we are not
16 ready to make a recommendation, because we're saying we have
17 to determine if this is possible.

18 One of the biggest barriers that -- I think we've
19 all heard the word, COSO-light, and the biggest barrier we
20 had for a long time is the auditors kept saying, you can't
21 make it any lighter than it is because we have to meet AS-2.

22 So now we're saying we'll take the auditor
23 attestation out of it. We're not asking people to be
24 required to do the AS-2 attestation, but just on something
25 significantly less than what they're used to doing.

1 So that's been a breakthrough. We'll take that
2 out. And now we will say to COSO, we hope to have a full day
3 meeting with him and his team. If we're not asking you to
4 try to water down AS-2 when AS-2 is the standard by which the
5 company's going to be held to, when we're really saying to you,
6 if you really could right-size this to small companies --

7 And we're not saying that what they have and are
8 delivering tomorrow is it. What we're saying to them is, are
9 we comfortable enough -- if we asked and made a
10 recommendation that the SEC look to you to deliver this, get

11 this done and get it delivered, would you be able to do it?

12 That's what we want to find out.

13 If they say we don't think we're able to do it,
14 then we'll decide is there some other body that can do it.
15 And that's why we're saying we're not ready to recommend.
16 Maybe we can't get there.

17 But everybody's who's come in, whether it's
18 investors or companies or anybody, has said, if you can get a
19 rational, reasonable standard to hold me to, then I can do
20 it. But right now you're holding me to a standard that just
21 doesn't work in the small company environment.

22 MR. WANDER: Drew?

23 MR. CONNOLLY: Janet, I'm happy to hear you say that.
24 I'm also, Ted, delighted that somebody recalled the
25 testimony, both of the fellow from COSO and the fellow who

1 used to be the chief accountant here at the SEC, who informed
2 us that they anticipated that Sarbanes-Oxley liked compliance
3 to cost \$91,000 per company and be able to be done with in a
4 week.

5 So my concern is that there have been a lot of
6 judgments made which have resulted in us being here trying to
7 right-size this and work it out and fix it and respond to
8 both the investor community as well as the small company
9 community.

10 So the one thing I'd caution you to do when

11 speaking with the professor from COSO and the representatives
12 of COSO, and this is not meant in any disrespectful way to
13 those august, well-intentioned, and thoughtful people, but
14 they have not had the benefit of the testimony that we've
15 had. They have not had anything more than an anecdotal
16 belief that maybe there's a problem.

17 I hate to, just as you hated to define it, what is
18 the nature of it, I'd hate to say that they may not have felt
19 our pain or the pain that we have, in fact, been privy to.

20 So while I certainly would pay attention to what
21 they have to say, I think we've already drilled down deeper
22 to some of the impacts than their mandate called for.

23 MR. WANDER: Alex?

24 MR. DAVERN: Yeah.

25 I'd just like to add to what Drew said here.

1 I do think, certainly from my personal opinion, I
2 think we should work with COSO. We should review their report.
3 We should talk to them.

4 But I personally do have significant lingering, I
5 guess not good feeling about the idea that we may end up with
6 a recommendation which would rely on the future actions of
7 another body to effectively execute once we've dismantled.

8 And I personally am more attuned towards making --
9 drawing bright lines around standards that are already known,
10 and Janet is obviously very familiar with my opinions on

11 this.

12 But I do think we should try and see where that
13 goes, but it is a nervousness on my part that we might end up
14 with a recommendation that another body solve the essence of
15 the problem at some point in the future, when we really can't
16 predict exactly what that outcome would be.

17 So thank you.

18 MR. WANDER: Rick?

19 MR. BROUNSTEIN: Yeah.

20 Just to sort of chime in, I think you've hit the
21 essence of what is the minority opinion back and forth in the
22 group, is can you accomplish this cost effective solution?

23 We think we owe it to ourselves to give it a try,
24 and I think that's where we're heading, and, you know if it's
25 something that the SEC selects a group, we want to talk to

1 COSO, but it doesn't -- and there's several groups that, you
2 know, may be the logical groups that could do that.

3 If they can't do it cost effectively, then, you
4 know, that's when the exemption starts to become more
5 logical.

6 MS. DOLAN: And I would just conclude on behalf of
7 our subcommittee, an answer to your question, Drew, is we
8 still are trying to say it's easy to say just exempt, and we
9 may end up there, but we feel that we have the duty to try to
10 create a solution that really works.

11 We think this is what should have been done first,
12 we think this should have been done first, which is create a
13 standard where everybody knows what it is, and then come in
14 and determine whether you've met it, but it wasn't.

15 So -- but we're just trying to say, can we now find
16 a way to try to recommend how to do that? We may conclude we
17 can't.

18 We may conclude it just can't be done, and then
19 we'll look at our options at that point.

20 MR. WANDER: Dick, did you --

21 MR. JAFFEE: Well, I think maybe Janet answered my
22 question.

23 I was starting to get lost here in terms of what
24 you're really looking for COSO or some other body to do.

25 I mean, it seems to me that, you know, in simple

1 terms, if you want an internal control system, you want one
2 that gives you the right answers to create your financial
3 statement and protects the assets of the company, but you're
4 looking for some much more elegant and comprehensive set of
5 standards that a company could look to and say, "Okay, I've
6 got a system and it fits their definition."

7 Is that what you're saying?

8 MS. DOLAN: Well, we live in a world now in which,
9 through 404, we have said that you really need auditor
10 attestation that you have the proper internal controls, and

11 so we've created a world in which people feel that's kind of
12 a necessary element of good business.

13 We're saying that doesn't -- that's not
14 cost-effective for a small company.

15 MR. JAFFEE: Yeah.

16 MS. DOLAN: We have to start with where we are,
17 which is we're taking something away.

18 We would like to be able to say to the marketplace,
19 good internal controls are really important, and in the world
20 before Sarbanes-Oxley, we would have said leave that to the
21 company to figure out what that is.

22 But we're not in that world. We're in a world in
23 which the public thinks that, or has come to expect that
24 you're going to have an external force coming in and
25 certifying what that is.

1 We're saying that's just not cost effective for
2 small companies.

3 But can we do something in which we actually say to
4 the investors, "But here's a level of confidence that you
5 should have in these small companies"?

6 And one way you would do that is to say we're going
7 to have the management actually assert that they have the
8 appropriate internal controls in place where you can rely on
9 their financial statements, but we don't tell them what that
10 is.

11 And we're trying to say can we create actually, you
12 know, a framework? And that's what a COSO or some other body
13 might be able to do.

14 We may not get there. We may have to say we're
15 just going to have to either exempt and live in the old world
16 in which you don't have any assertion of this, or we have an
17 assertion but we don't have a standard that you're holding
18 people to.

19 But we're just trying to see can we create some
20 kind of framework where we can help small companies say,
21 "Okay, if I can create those kind of controls, then I should
22 be comfortable with my assertion and the public should be
23 comfortable that my assertion means this."

24 So we're just trying to see is there a standard
25 where everybody can look at an assertion and say, I know what

1 that means." That's what we're trying to do, and we not get
2 there.

3 That's why I'm trying to say this is a work in
4 progress at this point.

5 MR. JAFFEE: No, no, I understand how you're
6 struggling with it, and I'm struggling to try and understand
7 these nuances.

8 And I guess the analogy in the financial statement
9 world would be that when you make the 302 assertion that
10 you're asserting that the statements are correct according to

11 the GAAP standard, is that what it is, and so going back to
12 what Mark said at the very beginning, there is no such
13 standard in the audit world.

14 MR. JENSEN: Yeah. Let me try to help you with it,
15 Dick.

16 If you go back to a lot of the testimony that we
17 heard, what I heard over and over again was that the auditor,
18 the public accounting profession was driving the cost because
19 of their need to meet a standard, an auditing standard,
20 AS-2, and the accounting firms believed that's what they've
21 audited to.

22 And I think what happened, and the dynamic that
23 grew out of that is that's how management got to the point
24 they were comfortable making their 404 assertion, because the
25 auditor was out there saying, "I need this to do the audit,"

1 and so management, out of that grew management's point of
2 view that, "Well, if I meet them, then I'm okay making this
3 assertion."

4 Once you take the auditor out of the picture and
5 you take AS-2 out of the picture, our fear is then the only
6 thing a smaller company could look to would be, even though
7 the auditor wasn't there, it would still be, "Well, this is
8 what they have to do in the larger companies so therefore,
9 this is what I would have to do down here."

10 The dynamic is you have to change that so that they

11 could look to something not necessarily as a safe harbor, but
12 they could look to a standard that would say, "This is
13 adequate for me to make an assertion."

14 I think, you know, we just have to see if we can
15 get there or not. Otherwise, I think, you know, we haven't
16 really done much for them other than remove the auditor --

17 MR. JAFFEE: I'll tell you, though, just to react
18 to that, that I guess if I had my choice of devils to deal
19 with, I might rather deal with the auditor attestation than
20 this murky world.

21 And I don't understand COSO, but I have had, you
22 know, just anecdotal comments about how thick the book is and
23 how heavy it is, and knowing the banking business, it's been
24 a big deal for a long time.

25 I'm thinking to small companies, at least you got

1 the auditors sitting in front of you to talk to them, but to
2 have to have this amorphous thing running around there called
3 COSO might be a big step backward.

4 MR. WANDER: Rick?

5 MR. BROUNSTEIN: Rick Brounstein.

6 Let me just take it to other extreme.

7 One of the presenters, Lynn Turner, a former chief
8 accountant, very active in the -- you know, has come up with
9 an aid that he claims that a CFO should be able to sit down
10 and basically in a day go through this process and be

11 comfortable in making a management assertion.

12 Maybe that's too far to the other extreme, but I
13 mean, to me, something along that line is very cost
14 effective.

15 I think you need to give us a chance and see what's
16 out there and see if we come -- you know, we clearly don't
17 want the 800-pound gorilla to tell us, you know, what makes
18 sense for a little company, a micro-company to do, or even a
19 small company, or else we won't have achieved the cost
20 effectiveness.

21 MR. WANDER: Actually, I'm going to show my age
22 now, but I think probably 20, 25 years ago, and maybe it was
23 actually -- and maybe, Dan, you'll remember this -- when the
24 internal control requirement first came in was, what, '77?

25 MR. GOELZER: '77.

1 MR. WANDER: '77.

2 There was some effort or discussion as I recall
3 about management, or at least a CEO signing some type of
4 certificate, and in fact some companies over the years since
5 that time have included in their annual report a management
6 certificate telling the shareholders and/or the investing
7 public that they have high standards and they're confident
8 that the financial statements are prepared in accordance with
9 GAAP, et cetera.

10 There was a big brouhaha about these certificates

11 at that time, and I will try and go back and recall it and
12 maybe share that with you, just to see what somebody else
13 thought some time ago.

14 Am I on target there or not?

15 MR. GOELZER: No, I think everything you've said is
16 correct.

17 I think the SEC had a proposal in the late '70s,
18 early '80s to require a management statement about controls,
19 and that's probably the brouhaha that you're referring to,
20 but I'm not aware of anybody having come up with any standard
21 or framework of the sort that we're talking about on the
22 subcommittee that would tell management how or on what basis
23 they ought to make that.

24 MR. WANDER: No, I see what you're saying.

25 MR. GOELZER: It was much more a free writing kind

1 of exercise in those days.

2 Then, of course, COSO a little later came into the
3 picture as the control framework.

4 MR. WANDER: Yeah, actually, the original COSO does
4a deal with
5 smaller and mid-cap businesses, and in my reading of it does
6 talk about applying different standards.

7 And I'll try and get that also for you, Steve,
8 because you might want to have, as you said, increased
9 disclosure; and I think you're right, Dan, it didn't have a

10 standard to apply to that report.

11 Mark?

12 MR. JENSEN: One other thing to think about -- this
13 is Mark Jensen -- or to look at, Herb, is in the original,
14 one of the original drafts under COSO, there was a complete
15 section on small companies and how it would be applied in
16 smaller companies, and that was eliminated in the final
17 draft, was taken out because of the concerns primarily of the
18 then Big Eight that we were creating two sets of standards.

19 So what was left within the final draft of COSO was
20 this principles based framework with a few paragraphs thrown
21 at the end of each one of the components that says, "Here's
22 what it might look like in a smaller company."

23 I think that one of the areas for us to start is to
24 go back, because there was a lot of work done on that, and
25 then it was eliminated because of the concern of the Big

1 Eight accounting firms not to have dual standards out there.

2 So I think there is some work that's already been
3 done in this area that we could take a look at.

4 MR. WANDER: Well, that's helpful. That's very
5 helpful.

6 Well, I think we've had a really excellent,
7 splendid discussion here. I think everybody has had an
8 opportunity to ask questions and to probe.

9 And again, I want to thank Janet and everyone on

10 the subcommittee, because you really have devoted your time
11 and attention and come up with, I think, a very sound
12 analysis, and whether we can get the next step, we will all
13 see.

14 But I think we're all cheering for you, at least.
15 Let me put it that way.

16 Any other comments before we move on?

17 It's now 11:25. Why don't we hear from one other
18 committee and then take a short lunch break and then come
19 back.

20 Would that be all right with everybody? Is that
21 agreeable?

22 Who would like to go next? I'll take volunteers.
23 Steve.

24 MR. BOCHNER: Steve Bochner.

25 I guess this will be a little anti-climatic after

1 the 404 Subcommittee.

2 (Laughter.)

3 MR. WANDER: I'm glad we did yours first.

4 MR. BOCHNER: I'll forge ahead.

5 So I think we, you know, we spent actually a fair
6 amount of time on these governance issues relative to the 404
7 attestation issue, so I've already talked about that.

8 I think, Herb, unless you tell me otherwise, I'm
9 not going to reiterate the areas of alignment that I covered

10 yesterday unless you'd like me to go through those again.

11 MR. WANDER: No, but at the end of your remarks,
12 why don't you ask if anybody has any comments on them, Steve?

13 MR. BOCHNER: Okay.

14 Maybe I will comment on the areas of alignment that
15 we have had some dialogue on and invite the members of my
16 subcommittee to chime in with additional or conflicting
17 thoughts on this.

18 We've discussed further this idea of the
19 accommodations provided under Regulation S-B, which are
20 modest but, you know, rather than three years audited
21 financials, two years, and a few other accommodations, and a
22 suggestion was made actually by Leroy, who was visiting our
23 subcommittee meeting this morning, that maybe we should
24 consider extending those accommodations not only to micro-cap
25 companies, but if we're really looking at trying to reduce

1 costs and increase efficiency without impairing investor
2 protection, should we extend those to all smaller public
3 companies?

4 In other words, would it somehow impair investor
5 protection if we allowed smaller public companies to not have
6 -- I think under that construct you would still have five
7 years financial results in summary form, but in terms of
8 getting the auditors in the loop, is a financial statement
9 three years ago really necessary for a smaller public

10 company, or is two years income statement and two year
11 balance sheet sufficient?

12 So I think that's -- I'm rolling that out to
13 describe some questioning and maybe some progression in our
14 thinking about just how aggressive we ought to be in looking
15 at those S-B accommodations.

16 I'll welcome it -- if anyone wants to chime in on
17 that, I'd welcome them. If not, I'll keep forging ahead
18 here.

19 MR. DENNIS: Steve, this is Leroy.

20 The one thing I think we also talked about was
21 whether, for investors, it made sense to provide comparative
22 balance sheets to those companies, so rather than the current
23 S-B standards, where you have one balance sheet, two income
24 statements, we'd go to a two and two standard, and I don't
25 think that would add any cost to complying with the S-X or

1 Regulation S-B, and certainly wouldn't require any further
2 auditor involvement than we require right now, and probably
3 provides better financial information for investors out there
4 at very little cost.

5 MR. BOCHNER: Yeah. Thank you.

6 MR. WANDER: Rick?

7 MR. BROUNSTEIN: Yeah, Rick Brounstein.

8 Just a quick reiteration that I've been filing
9 under an S-B for a while, and we've always filed two and two,

10 and that's -- there's no more work to be done to do it that
11 way, so why wouldn't you?

12 The other thing, and maybe it ties into what you're
13 doing, but some of the negative requirements on the S-B tend
14 to do when you're doing registration statements, and the fact
15 that you can't incorporate by reference and such as that.

16 So hopefully, we're going to keep the good and not
17 some of the more onerous provisions.

18 MR. BOCHNER: Yeah, we have, as it's now
19 formulated, a separate recommendation that we would extend
20 S-3 availability and forward incorporation by reference
21 privileges to smaller public companies on the theory that if
22 Internet accessibility exists as widespread and the
23 information is there, why should smaller public companies be
24 deprived of referencing that and we only allow larger public
25 companies to reference that?

1 So I think we're still interested and supportive of
2 that idea.

3 You know, another topic that has surfaced is you
4 now, and perhaps this may not be popular with the SEC, we'll
5 have to let them decide this, but today if you miss a filing,
6 even if it's attributable to, say, problems with 404 that
7 we've identified, you are put in an S-3 penalty box for a
8 year, so instead of being able to use the short form, you now
9 have to use the long form.

10 And I guess we have questioned that within our
11 subcommittee, you know, why -- does the punishment fit the
12 crime?

13 In other words, why make -- if the information is
14 already there, why are we making the company spend more of
15 the shareholders' money to do a longer form rather than a
16 shorter form?

17 Maybe there should be some other sort of remedy, if
18 you will, and maybe it is time to get rid of the timely filed
19 requirement and simply, you know, you're S-3 eligible if
20 you've been reporting for a year, and as of the date you file
21 the S-3, you're timely.

22 But, you know, we'll have to talk to -- I'm sure we
23 may hear from Enforcement and the Division about whether or
24 not that's a good idea and whether or not that penalty box is
25 an effective stick that they use to make sure companies file.

1 MR. WANDER: Well, thinking about that, I mean, if
2 you have some sort of increased disclosure, maybe the more
3 appropriate standard would be some sort of satisfactory
4 certifications under 302 might be, in fact, more helpful to
5 investors than having timely filings, just as a timely
6 filing.

7 MR. BOCHNER: And I think today, Herb, under 302,
8 you're required to talk about designing disclosure controls,
9 and I think if you're missing SEC filings, I would question

10 whether you can take the position that your disclosure
11 controls are effective, so you may even have a context in
12 which to address your point today.

13 MR. WANDER: In fact, the certificate, as I recall,
14 does say that you have controls that will permit you to
15 timely report.

16 Good idea.

17 MR. BOCHNER: So I think on the areas of alignment,
18 I'm not going to cover anything else there that I reiterated
19 yesterday.

20 We have kicked, everybody will be happy to hear,
21 the materiality issue over to the accounting subcommittee
22 where it properly belongs, and I think actually Leroy has
23 made some progress on that, and I'm going to leave that to
24 him to talk about.

25 The only other area that I think we want to talk

1 about is this beneficial record holder issue, and we did
2 continue to discuss that.

3 This is the problem with the form over the
4 substance.

5 If there's a number that's in place today that
6 requires one to register, and also a different number of --
7 number of shareholders we're talking about -- and a different
8 number that allows one to de-register, that number can be
9 gamed if we're talking about record holders and not

10 beneficial holders.

11 So the idea is perhaps to move to less of a form
12 over substance construct and move to beneficial holders, so
13 you actually look at the real shareholders for purposes of
14 determining at what point do you cross a threshold and you're
15 large enough that you should be filing reports with the SEC,
16 and similarly, when is the real number of shareholders small
17 enough that you should no longer have to file reports?

18 So the question is, where do you draw that line?
19 And we have had some thoughts about that.

20 I think, just to throw some ideas out there, we've
21 had discussions around the total asset number perhaps moving
22 up from 10 million to something like 15 to 20, although those
23 are just thoughts, and perhaps moving up the shareholder
24 number, which would now be beneficial, not record, to
25 something like 1,000 to 1,500.

1 We're very mindful, as we say that, of the impact
2 this could have on a lot of companies, and so we need more
3 data on that impact, and I think the SEC is going to try to
4 help us to, as best they can, get that data, and if we do do
5 something along those lines, we're certainly going to have to
6 have a phase-in period for issuers on both sides to be able
7 to plan for it, to see it coming, and not just put something
8 in place immediately.

9 So I think that, unless members of my subcommittee

10 have other thoughts they want to talk about, I think that
11 summarizes our discussions.

12 MR. WANDER: Dick or Pastora? Any --

13 MR. JAFFEE: Well, just to beat my dead horse to
14 death here a little bit, the director independence issue, and
15 Dave mentioned it -- you know, Steve keeps telling me that
16 the rules are clear and that if we tried to clarify them
17 further we'd run into the Delaware court issues, and I keep
18 thinking that the rules are kind of silly.

19 The part of it where you can't pay anybody anything
20 on a consulting fee -- first of all, you could game that by
21 just creating a board committee, if you wanted to, in the
22 name of whatever the consulting was and say it's a board fee,
23 but that doesn't really feel good.

24 So my guys said, "Why don't you ask for a safe
25 harbor with a specific dollar limit under which you would

1 still be independent and over which you would be deemed to be
2 unindependent?"

3 But Steve keeps telling me that it really isn't
4 doable that way, and I defer to his greater knowledge.

5 So I don't know, that's just an issue that we've
6 banged around a little bit.

7 MR. WANDER: Pastora?

8 MS. CAFFERTY: Let me say that I think this
9 argument of the difficulty of finding independent directors

10 is a red herring, but it's a very dangerous red herring
11 because the whole idea of independence is that the company
12 will be forced to go outside those people that they know.

13 And I must say the most salutary effect in the
14 boardroom, and again I'm talking about mid and large sized
15 companies, is that for the first time, really, in the last
16 five years many companies who have basically recruited
17 directors based on who the CEO knew or the board members
18 knew, you know, sat down, very good faith efforts -- I'm not
19 -- but it's who we all know, and we come down with a short
20 list and then we make it shorter. We interviewed them. We
21 took it very seriously. But there was no stranger in the
22 room.

23 Thanks to, I think, the push for truly independent
24 directors, we've been forced to look outside whom we know,
25 because there is a shortage of directors.

1 And this may be a boon for the search firms, but
2 the fact is that it is very refreshing to have someone in the
3 boardroom that you've never met before in your life after
4 you've, you know, interviewed them, you're comfortable, they
5 fit with the board, you know.

6 There's more proactive behavior on independent
7 board members, outside board members.

8 It doesn't mean the CEO is not included in some of
9 the interviews, but the boards have really taken a very

10 aggressive stand on this, and to me the benefit is that you
11 have people who are not familiar with the company, who are
12 not familiar with everybody sitting in the room, asking
13 questions, and the beauty of this is that you get a very
14 refreshing, different point of view.

15 I cannot believe that small cap or even micro-cap
16 companies in the smallest towns in America cannot find
17 perfectly intelligent people, knowledgeable people, good
18 strategic thinkers who may be on a local high school faculty
19 rather than sitting at another company, and may not be
20 included in this, but can think and can ask questions.

21 So I'm very -- I think there's great salutary
22 benefit to having independent directors well beyond the
23 proscription. You really get different minds in the room and
24 a variety of thought in the room.

25 I also have a lot of trouble, and Dick knows this,

1 with the exception from fees.

2 You can game any system, but the fact is that the
3 idea that no director is paid extra for whatever he performs
4 for that company I that is again a very salutary thing.

5 Boards increasingly are going to retainers. They
6 don't have to be huge retainers.

7 There's a lot of status and privilege serving on a
8 board, and I'm old enough to remember where \$25,000 for a
9 Fortune 100 company was a very acceptable fee.

10 Now, I'm not suggesting in today's world -- this is
11 25 years ago -- but you didn't go on it just for the fee.

12 So I urge all of us on the committee to take a wider
13 view of independent directors and a wider view of a certified
14 financial expert.

15 Someone who is experienced in drawing up budgets,
16 who oversees a non-profit wisely as well as a for-profit can be
17 a certified financial expert, and they're being certified on
18 boards by outside counsels constantly of very large
19 companies, so I'm sure it can be happening in a micro-cap,
20 too.

21 So I just get a little uncomfortable when we focus
22 so much on the difficulty of finding independent directors.
23 The difficulty is finding independent directors whom we know,
24 and that is a difficulty, but there's a lot to be said for
25 going outside of this.

1 MR. WANDER: Yes, Drew, and then --

2 MR. CONNOLLY: Pastora, while I fully understand
3 your position, I guess as the guy who carried the red herring
4 into the room --

5 (Laughter.)

6 MR. CONNOLLY: -- I'd like to have an opportunity
7 to just explain a little bit about my herring.

8 The fact is that for many, many, many micro-caps,
9 the intersection of directors' fees and the D&O insurance

10 that we have not really talked about here too terribly tough,
11 but in my micro-cap community, it becomes a significant
12 number, and has obviously increased as Sarbanes-Oxley has
13 come to the fore and the fear of the insurers, maybe justly,
14 about potential claims has obviously market priced and D&O
15 up.

16 I have no problem. Actually prior to being
17 appointed to this committee, I'm in roomful of people I
18 didn't know and I would be delighted to work with virtually
19 everyone here once the committee is over.

20 So I don't think we have a concern about working
21 with strangers, per se --

22 MS. CAFFERTY: I'm not suggesting you do.

23 MR. CONNOLLY: -- but I would have a real concern
24 if I had to recruit the high school basketball coach to help
25 me run my manufacturing business because he was -- you know,

1 the cost of a true financial expert director, given the
2 potential liability that everybody is now facing and the
3 experience they're having in being sued, I'm not sure what I
4 would have to pay that high school basketball coach, but if
5 he were informed as to his potential liability, I think he'd
6 probably price himself in a way that would be stressful to
7 me.

8 MS. CAFFERTY: Drew, we could go on, and we have to
9 have this discussion, but it's only throwing out there

10 something for the committee to think about, and in my
11 experience, financial experts on boards are not paid any more
12 than any other director.

13 And I wasn't suggesting a high school basketball
14 coach, although there may be one out there that's wonderful
15 for this, but all I'm saying is think this through very
16 carefully, because we're not -- maybe we should just limit it
17 to the audit committee so it's three, but I really think the
18 value of credibility with the public of having truly
19 independent directors is a real one.

20 But, you know, and I'll drop it for the time being,
21 because I'm sure the committee will continue to consider
22 this.

23 MR. CONNOLLY: I absolutely hear what you're
24 saying, and I guess maybe I'm not aware of what directorial
25 compensation is in the real world, but I know that I doubt

1 that I could find a director for \$25,000 for my companies,
2 and I don't think I'd be insulting enough to offer them that.

3 So all I'm saying, and there's nothing about
4 independence that's not healthful, and clearly that is one of
5 the areas of Sarbanes-Oxley that I think any one of us who is
6 interested in good clean markets would support, but while we
7 believe that the universe of people who would be pleased to
8 work as directors for companies, I don't see it in my end of
9 the marketplace.

10 MR. WANDER: Well, let's move on.

11 Leroy?

12 MR. DENNIS: I just want to add two comments.

13 Leroy Dennis.

14 One is, I support what Pastora said. As far as
15 from an auditor's standpoint, I can't think of any one thing
16 that we've done over the past five years that has increased
17 audit quality than having an independent board member that
18 the auditors can go to.

19 The other thing I heard here in this banter back
20 and forth is that maybe we're not addressing the issue.

21 Maybe the issue we need to address is similar to
22 the issues that Janet has brought up about auditor liability
23 concerns and how that's driving the process, and maybe we
24 need to think about board liability and how should that be
25 construed in a legal context of what is the liability

1 appropriate for a board member that gives best efforts, not
2 fraudulent, but is there some kind of relief that we can
3 recommend or provide to audit board members that are giving
4 their best efforts?

5 I'm not after to protect people that are bad, but
6 how do we protect people that are trying to do a good job?

7 MR. JAFFEE: Herb, can I comment on that?

8 MR. WANDER: Certainly, Dick.

9 MR. JAFFEE: You know, I think that is a very, very

10 important point, and it's not just -- we've talked about it
11 in terms of recruiting new directors, but I think maybe the
12 bigger issue really is existing directors who now are in a
13 world in which they know there's some higher standard out
14 there that they may potentially be held to.

15 And it's very analogous to what Mark said about the
16 404 thing. They don't really know precisely what that
17 standard is, so everybody is around hawking best practices.

18 There's going to be a thing on compensation in a
19 couple of days on a webcast where a bunch of well-known
20 directors are going to talk about compensation.

21 But I think that's a hugely important area. Now, I
22 don't know how you deal with that, again, because the real
23 big gorilla in the room is the legal system.

24 MR. DENNIS: I was going to push that to you guys,
25 so --

1 MR. JAFFEE: Yeah, sure.

2 But I can tell you, and I could name names of
3 people who were perfectly comfortable in their roles five
4 years ago, and today are real nervous and there hasn't been
5 anything changed in the company's situation, it's in the
6 external environment in which they feel they're operating.

7 MR. WANDER: I will give you one vignette from one
8 of my clients.

9 When the financial expert provision became

10 effective, the board of this particular client said, you
11 know, "Do any of the members presently satisfy that
12 requirement or meet that standard?" And in fact, they did.

13 But the board sort of said to itself, and this was
14 an open discussion, that they thought for board protection
15 the board should make sure there was a financial expert on
16 the audit committee that was frankly not a retired audit
17 partner of an audit firm, but rather a currently sitting CFO
18 who knew how to operate in the trenches, and the board felt
19 that that was more protection for the other members, which
20 -- if we're looking for to be helpful.

21 So let's move on, though.

22 Any other questions for Steve? Any other -- yes,
23 Mark.

24 MR. JENSEN: Yeah.

25 I just kind of want to come back to this point

1 again, because it comes up over and over again, and I feel
2 like there's another participant on this committee that you
3 can't talk to, and that's the plaintiffs' bar, because every
4 time something comes up, we actually are talking about the
5 plaintiffs' bar and what happens and how to protect
6 ourselves.

7 And I'm wondering, is there nothing that can be
8 done out of this committee in that area? I mean, even to
9 take a minor step, I think would be important as basically

10 getting a ball rolling and trying to stop this endless
11 discussion around, "Well, if we do that, we've increased
12 people's liability."

13 You know, because it seems like --

14 MR. WANDER: Well, we could recommend another
15 advisory committee.

16 MR. JENSEN: No, thank you.

17 But I mean, it just seems like common sense goes
18 out the window, and --

19 MR. CONNOLLY: Loser pays.

20 MR. WANDER: That was Drew who said "Loser pays."

21 Jim and I will think about how we could insert that
22 at this frankly late date here.

23 I'm not trying to minimize the issue. Congress
24 went through this when they passed the Securities Reform Act,
25 what, seven, eight years ago, and it's a highly charged area,

1 et cetera, and there may be particular reasons, I personally
2 believe, in the accounting profession that it might be
3 appropriate.

4 I think the law on directors, I think what's
5 happened is all these seminars happen, and frankly, lawyers
6 go out and give scare tactics to their boards and tell them,
7 "If you do these 101 things, you'll be all right."

8 Well, you know, if you're the director, you sort of
9 say, "I can do 80, but I can't do 101."

10 And the result is, it's sort of a piling on, and I
11 think frankly the -- both the SEC and the PCAOB criticized
12 the accountants for not using enough judgment in their May
13 releases.

14 Some of that rubs off on the lawyers, as well, in
15 using judgment to tell people what their real risks are if
16 you actually do pay attention, go to meetings, and try and
17 come up with the best decisions.

18 Yes, Janet.

19 MS. DOLAN: Herb, this coming from the committee
20 that wants to solve a problem, I'm not sure we can solve that
21 problem, but I do think it would be good for us in the
22 preamble that we start connecting some things like
23 competitiveness, risk aversion, and saying that those are the
24 things you do not want to happen in your capital markets, is
25 to become risk adverse, that it is a really important element

1 of the success of our capital markets that we understand that
2 risk is an element of it, and in this competitive world,
3 capital can move in a nanosecond.

4 So I mean, I do think in the preamble or something
5 we should tie some of these bigger themes that we can't
6 solve, but we should at least say are the environment in
7 which we're making our recommendations.

8 MR. WANDER: Drew.

9 MR. CONNOLLY: Janet, I'd be delighted to work with

10 you on drafting that language, and I'm sorry that you jumped
11 that comment that I was hoping to make today, because the
12 reality is that you cannot legislate out all fraud, all
13 fraud, bringing it down to the point where we're, you know,
14 implementing a marketplace that's not possible.

15 It's part of -- it's kind of a perversity, but a
16 little bit of fraud, unfortunately, keeps everybody else
17 honest because of the ability to focus that question.

18 And I'm not buying into the idea that we should be
19 supporting that, but clearly, in the micro-cap section of the
20 world, every financial advisor who is prudent is dictating
21 that this is a risk-oriented portion of the market, whether
22 the risk is any more out-sized than some of the majors, as
23 we've seen over the years.

24 I got a statistic that was very interesting the
25 other night. Every micro-cap company, as we've defined them,

1 in terms of total market capitalization equals one Worldcom.

2 So the question of whose money is being lost and
3 where that money is being lost, one could argue that since
4 Worldcom qualified for pension fund investments and the
5 micro-caps, in most circumstances, do not, the impacts are
6 even more outsized.

7 So risk assumption is something we should actually
8 be encouraging.

9 That's the basis of this country. It's how the

10 country was settled. It's how the country was built. And
11 I'd be delighted to help you work on some of that language.

12 MR. WANDER: Jim?

13 MR. THYEN: Yeah. This is Jim Thyen.

14 Steve, does the committee have anything additional
15 to share with us on the access equals delivery area that I
16 know you've been debating and talking about a lot?

17 MR. BOCHNER: Jim, I think we still continue to
18 very much like and support that idea, that clearly there will
19 come a time -- and I think we are suggesting maybe it's now,
20 and I think the SEC in the securities reform release took
21 baby steps in this direction with respect to the final
22 prospectus delivery -- there will become a time when we say,
23 okay, Internet accessibility is widespread enough that we
24 don't need to stuff mailboxes all across the country with
25 proxy statements and annual reports, that most of us actually

1 go on line, subject to having appropriate protections for
2 those shareholders that still desire paper copies.

3 And you've got to have those protections. It's got
4 to be at no cost. You've got to build in time.

5 But at some point, you know, if our mantra here is
6 reduce costs without impairing investor protection, while
7 this isn't an area of great cost, we've identified it as an
8 area where smaller companies are disproportionately affected
9 by having to do all this printing, you know, this printing

10 job, which largely ends up in recycling bins, we think.

11 And therefore, you know, we really would like the
12 SEC to consider extending the access equals delivery model to
13 other SEC filings, so I think we're very much in favor of
14 making that recommendation to the committee and then
15 hopefully to the SEC.

16 MR. WANDER: Did you have -- thank you.

17 MR. BOCHNER: Jim, can I add one thing to that?

18 MR. WANDER: Certainly. Certainly.

19 MR. BOCHNER: So, Bob just reminded me, quite
20 correctly, that we should also not forget to talk about
21 EDGAR.

22 There is some suggestion -- you know, I think EDGAR
23 has worked well. I think when it was adopted, it was, you
24 know, very forward thinking, ahead of its time.

25 But there is some suggestion now that, you know,

1 why is it that public companies, particularly smaller ones,
2 have to go to the printer and pay all this money to get
3 EDGARized, and, you know, isn't -- and I'm going to be the
4 last person in the world to suggest the technical solution to
5 this.

6 But shouldn't there be some easier mechanism,
7 through e-mail or a common format or something, that allows
8 companies to more cost effectively get their SEC filings done
9 without having to seek outside help to simply transmit a

10 document that they've already got internally.

11 So we haven't figured out exactly how to frame
12 that, but I think that's another element of this efficiency
13 idea, along with access equals delivery, the incorporation by
14 reference idea, and just trying to ease the system where it
15 doesn't -- where this seems like low-hanging fruit, where we
16 can make these changes, save some costs, and we really don't
17 think investor protection will be impaired.

18 MR. WANDER: Okay.

19 MR. CONNOLLY: Steve, that clearly is an overhead
20 expense.

21 One of the things, I was concerned enough about
22 this, as recently while in San Francisco, went to a banking
23 conference, ran into an executive from EDGAR Online, and
24 asked them -- Susan Strausberg's company -- asked them would
25 they, under any other circumstance, be able to extract the

1 data, this new XBRL language, which allows financial report
2 information to be extracted, manipulated, spreadsheeted, et
3 cetera, would that, under a non-EDGAR circumstance, would
4 they be able to do that?

5 And actually, I don't think he knew the answer.

6 And I know that that has been raised to us here by
7 Kathleen, so there must be somebody within the organization
8 here who might be able to give us both the cost overall to
9 comply with EDGAR, and also whether or not the technology

10 exists to do something other than EDGAR.

11 MR. WANDER: Okay. Any other comments, questions,
12 ideas for Steve?

13 (No response.)

14 MR. WANDER: If not, it's about five minutes to
15 12:00. Why don't we break until 1 o'clock -- is that enough?
16 -- come back for the last two reports, and then discuss next
17 steps? Is that all right with everyone?

18 We're adjourned until 1 o'clock. Thank you.

19 (Whereupon, at 11:55 a.m., a lunch
20 recess was taken until 1:02 p.m.)

21 MR. WANDER: It's now a few minutes after 1
22 o'clock, and we're missing a few people who I know are still
23 here.

24 So why don't we wait just a couple of minutes, and
25 those of you who are listening on the web page, we'll start

1 as soon as we get a few more people around the table.

2 (A brief recess was taken.)

3 MR. WANDER: A few more of our committee members
4 have arrived, so we can begin the meeting in a couple of
5 minutes.

6 (A brief recess was taken.)

7 MR. WANDER: All right. I think we have a
8 complement of everyone. Let's see.

9 Kurt was here a minute ago. We keep losing and

10 gaining people.

11 Okay, here's Rick.

12 Why don't we begin, however. A few members have
13 had to leave, primarily Janet Dolan, for those of you who are
14 listening, and Dick Jaffee will be here in a minute.

15 Has anybody else left? I don't think so.

16 Oh, Alex Davern, yes.

17 So I think we should move on, and the next
18 subcommittee, why don't we go to you, Leroy?

19 MR. DENNIS: Okay. Leroy Dennis from the
20 Accounting Subcommittee, and I've got Patrick here with me.

21 We basically talked around the four or five areas
22 that we still have some divergence on, and so I'll go through
23 those real quick.

24 SAB-74, when we discussed that, we decided there
25 really was no need for revisions to that standard to be in

1 compliance, or with the spirit of our recommendation to
2 extend the implementation date for accounting standards for
3 micro-cap companies, so we'll be making no recommendations
4 there.

5 Steven has already talked about the predecessor
6 auditor and the 10-Ks.

7 We really were addressing that issue on the three
8 years versus two years financial statement requirement in an
9 effort to increase the competition and reduce the cost to

10 change auditors, and we talked about whether we should change
11 the requirements for predecessor auditor involvement in a
12 10-K filing.

13 Given that we would go to a two-year -- recommend
14 going to a two-year standard versus a three-year requirement
15 for financial statements, we don't think that's much of an
16 issue anymore and would just recommend alignment with Steve's
17 recommendation on a two-year balance sheet income statement,
18 and nothing further on our part with that.

19 From the PCAOB registration standpoint and the
20 comments I made yesterday requiring some minimum standards
21 for registered accounting firms to practice in front of the
22 SEC, the more we talked about that, I guess I got convinced,
23 albeit with maybe some arm twisting, but convinced that we
24 need to let the PCAOB do their job and not require any
25 minimum standards from the auditors, but that the PCAOB will

1 do that through their inspection process, and that the market
2 will eventually sort that out.

3 I would -- I still want to explore the possibility
4 of some kind of annual education requirements for people to
5 practice in front of the SEC.

6 As you may or may not know, the AICPA quality
7 centers require a certain level of training every year to
8 audit a pension plan, they require a certain level of
9 training to audit government entities under Yellow Book, but

10 as far as I know, there's no specific requirement to attend
11 any kind of training to audit General Motors; so that seems a
12 little bit of a disconnect there, that we ought to have some
13 kind of minimum requirements for auditors.

14 On the FASB structure with the small business,
15 we're going to talk to George Batavick about these at and get
16 his input before we make any recommendations on that, in that
17 light.

18 And then we probably spent the majority of our time
19 talking about materiality in financial statements and the
20 number of restatements that are occurring.

21 Whether that's good for the market, whether it's
22 good for investors, I think is subject to some debate.

23 Obviously, if the financial statements are
24 materially wrong, they need to be fixed, but we think we're
25 under a perfect standard right now for financial statements

1 as opposed to a materiality standard when it comes to looking
2 at errors in prior financial statements, and we're also, we
3 think, moved to a quarterly materiality level so that the
4 real test is based on a materiality level on a quarter from a
5 practical standpoint of what's going on in the market.

6 That's resulted in several restatements, that I
7 think we all have a consensus that under the same set of
8 rules five years ago would have not resulted in the same
9 number of restatements that are going on today.

10 We think that doesn't do well for investor
11 confidence in the markets, that restatements should be
12 reserved for things that are material enough to deserve that.

13 We're not ready to make a recommendation in that
14 area, but we did meet with the SEC staff.

15 And Gerry, I just want to just interrupt for a
16 second, because every time we've asked the SEC for anything,
17 they have just been extremely, extremely helpful for us.

18 You know, we arranged a meeting yesterday afternoon
19 and got people -- you know, Scott Taub came down and met with
20 us, and I know he's a busy guy, and that's just been -- I've
21 experienced that over and over again, and I'm just really
22 complimentary of your people here.

23 But back on point a second.

24 The two areas we want to look at are, it seems like
25 there's been situations where an error is discovered in a set

1 of financial statements, and in each individual financial
2 statement, be that quarterly or be that annual, the number is
3 deemed not material, but when you try to correct the error
4 that the cumulative catchup of that is material to any one
5 quarter.

6 And so we want to explore that as to what is the
7 right answer for the markets, and how that should be treated
8 in a financial statement, whether that -- I think right now
9 those financial statements are being restated for

10 theoretically immaterial amounts in each quarter.

11 The other probably more difficult question is
12 should we go to an annual or a quarterly level of materiality
13 for setting a materiality standard?

14 And I think there is divergence of views in our
15 group. We have some thoughts as to which way we would want
16 to go, and we need to get some more, probably some more input
17 from the staff on that issue before we would make a
18 recommendation.

19 In that same light, I would ask for input from
20 anybody else on the committee if they have some thoughts on
21 that issue, because it is kind of like the 404 comments of
22 "Tastes great" or "Less filling," I think. It seems to be on
23 one side or the other.

24 So that's where we're at, and Patrick, do you have
25 anything else you want to add to our group?

1 MR. BARRY: (Shaking head)

2 MR. DENNIS: We will be working with the SEC to
3 develop a recommendation surrounding materiality, and then as
4 far as the two year versus three year statement, I assume
5 we'll just let that go into your committee as far as a
6 recommendation, but with our support.

7 MR. WANDER: Any comments, questions?

8 Dave.

9 MR. COOLIDGE: Yeah. Dave Coolidge.

10 On the materiality thing, at least this is just my
11 general observation, is that you're right, there have been
12 more and more of these restatements, and it does wreak havoc
13 in the marketplace, because when it's announced, generally
14 there's not an appreciation for the difference between what's
15 really material and what's, you know, not so material.

16 But to the extent that you can get away from
17 quarterly materiality, I think it's better, you know, that
18 annual materiality clearly is something you have to deal with
19 and flag it, but I think it's really created a lot of
20 confusion in the marketplace as to, you know, what's really
21 going on at these companies when they have a restatement.

22 Sometimes it's really a tempest in a teapot, and
23 sometimes it's a big deal, but nobody can tell anymore what's
24 a big deal and what's not a big deal.

25 MR. DENNIS: Yeah, we agree.

1 I think the other thing that we need to look at
2 with this is the format of quarter restatement.

3 Is it appropriate to re-file prior financial
4 statements every time you change a number in a quarterly Q,
5 or can, if you're just doing comparative statements, can you
6 just correct in your current quarter with appropriate
7 disclosure of what's going on and is that a better method for
8 the Qs, anyway, to deal with that?

9 I think we all agree that if we have an error in an

10 annual filing that's material on that annual financial
11 statement, that we got to re-file the Ks and make
12 everything right.

13 There's a little bit less agreement on the Qs, on
14 how to deal with those.

15 MR. WANDER: I do know that when you have to
16 restate over a longer period of time you can get by with
17 restating them all together in one document rather than
18 re-filing a bunch of 10-Qs, which is, I think, actually
19 plainer and concise-er and more easily readable by the
20 investors.

21 We had asked Huron Consulting to appear in New York
22 two weeks ago.

23 Huron does the annual restatement studies. They
24 have quite a bit of knowledge base there. And unfortunately,
25 their top people were all very busy that day.

1 But if you would like to converse with them, Leroy,
2 I can put you in touch with them.

3 MR. DENNIS: That would be great.

4 MR. WANDER: And, in fact, then they could perhaps
5 even make a written submission to the whole committee so we
6 can have that available to the committee and the public,
7 because they're very interested, and they have done a lot of
8 work and have a big database, and have formed some judgments
9 on restatements.

10 MR. DENNIS: That would be great, if we could get
11 that, so if you want to arrange that --

12 MR. WANDER: Yeah, I will do that tomorrow.

13 MR. DENNIS: Thank you.

14 MR. WANDER: Rick.

15 MR. BROUNSTEIN: Rick Brounstein.

16 I'm back on the first subject that you were talking
17 about, minimum audit standards for practicing.

18 Just thoughts, and maybe I'm in the middle of it.

19 I don't know, I think we had talked a little bit
20 about whether or not we could recommend some body be formed
21 that would be some national level expertise.

22 I mean, if you take a look at the bigger accounting
23 firms, they all have their national offices.

24 If you look at the little accounting firms that all
25 these smaller companies are relying on, if they want to get

1 it right, and then they have four or five public companies,
2 they're stretched.

3 We have, you know, just personally, we have a small
4 firm that happens to have an affiliate relationship with BDO,
5 but BDO is the only company that I know that is willing to
6 qualify, you know, a smaller company, and allow them
7 basically access to a national office.

8 I don't know if it's within our purview or how one
9 would go about it, but it seems to me that that organization

10 would not only help qualify these people, but give them the,
11 you know, the help in tackling a lot of the more complicated
12 accounting rules that are coming out that they probably can't
13 get right on their own.

14 MR. DENNIS: Yeah, I think there are other firms
15 out there that provide networks of like BDOs that do that,
16 but one of our recommendations at the SEC, I don't know
17 whether it needs to be inside the SEC or outside the SEC, but
18 some kind of help desk, like what you're saying, for both
19 smaller CPA firms and for registrants to avail themselves of
20 -- you know, where they have a place to ask questions.

21 My sense is something outside the SEC would be less
22 threatening to someone, and there may be less of a -- you
23 know, there might be a hesitancy to call the SEC with a
24 question. I don't know that.

25 MR. BROUNSTEIN: I mean, to me, it's not simple,

1 because there's liability issues.

2 I mean, you're actually looking to somebody, you
3 know, to give you the right answer.

4 MR. DENNIS: I mean, there are groups like the old
5 Andersen Accounting Research Manager -- they have a practice
6 called Accounting Research Manager.

7 I don't believe the old Andersen, I forget the name
8 of the consulting firm, but they will not advise people on
9 public companies because of the liability around it, but at

10 least on private companies, I know they will advise on
11 accounting standards and implementation and give their
12 advice.

13 I don't believe they do that for public companies,
14 but that is -- those type of services I believe are out
15 there. They are not cheap for people to subscribe to, but
16 they are out there.

17 MR. WANDER: Mark.

18 MR. JENSEN: This is Mark Jensen.

19 Leroy, a couple of questions.

20 I want to go back to materiality and then I want to
21 come back to another question I have.

22 But have you thought at all -- I tell you, I'm a
23 little worried about redefining materiality again. I kind of
24 think materiality is pretty well understood.

25 It seems to me the issue is more around, when there

1 is an event, how that ultimately gets communicated to the
2 marketplace.

3 And have you thought at all about having maybe
4 different requirements for different size companies?

5 And the reason I say that is, materiality, I always
6 like to say materiality with a client, whenever we got into
7 those arguments, was, immaterial means neither you nor I
8 care.

9 So if you don't care, then that's fine, and maybe

10 we should just do it right.

11 If you do care, then it means it's material to you,
12 now it's material to me, and we got another debate going on.

13 And that really is what materiality comes down to
14 in the end. That's what the word means. It's -- you know,
15 forget how you define it. It means it's immaterial.

16 So I -- but I'm sensitive to the fact, in smaller
17 companies, going back and redoing financial statements, when
18 you don't have an analyst following the company and you don't
19 have this kind of, you know, treadmill that you're on in the
20 bigger companies with analysts, that you got to make
21 earnings, you got to make your number, and things like that,
22 I think an auditor is going to have a hard time.

23 It's not my job to figure out how the market is
24 going to react to an item, and I don't think we want the
25 auditors making those decisions. I don't think the auditors

1 want to make them.

2 But in smaller companies, it seems, you know, our
3 first mantra should be, "Do no harm," and it seems to me
4 there's no harm in maybe letting them have an easy way to
5 catch up.

6 I mean, have you talked about it that way at all?

7 MR. DENNIS: Well, we've talked about -- and I
8 would characterize what we talked about as not redefining
8a materiality, but

9 clarifying whether or not materiality should be based
10 quarterly or annually, and there is some disagreement as to
11 if you have something that's potentially material to a
12 quarter number, whether or not that it rises to the level of
13 materiality on an annual basis.

14 We did talk quite a bit about process, and, you
15 know, is there a different method of, quote, restating when
16 you have a situation where something is maybe material to a
17 quarter but not material to an annual financial statement.

18 We talked about whether or not you could catch up,
19 you know, and does it make a lot -- does it really help the
20 public to re-file a quarterly Q that's eight quarters old or
21 seven quarters old, or are you better off just to discuss
22 that in your annual filing and then when you're presenting
23 current year 10-Q information, make sure that you compare it
24 to accurate numbers.

25 So we talked a lot about process, and does that

1 work.

2 We really didn't talk so much about whether big
3 companies should have a different method of doing this than
4 smaller companies. My guess is the more analyst coverage you
5 have, the more you have to consider whether to re-file those
6 Qs or not.

7 And we're really just -- I mean, Steve handed us
8 this late last week, and so we've had about an hour to talk

9 about it, so we're really just kind of scratching the surface
10 a little bit on this.

11 But all these things are things we've talked about,
12 and we don't have any answers for yet.

13 And I would value a lot of your input, if you --

14 MR. JENSEN: Yeah. I'd be glad to talk to you
15 about it.

16 The other question I have that I still think is --
17 I know you talked about it before, but I haven't hear you say
18 anything about it today, is on this whole area of auditor
19 independence and whether, in a smaller company environment,
20 you know, kind of giving smaller companies maybe a little
21 more of a break or the auditor an ability to do a little bit
22 more, is that just off the table now?

23 MR. DENNIS: That's pretty much off the table right
24 now as far as we're concerned.

25 We talked a lot about that, went back and forth

1 between members of our committee, spoke a lot to auditor
2 representations around the firm, around the company, or I'm
3 sorry, around the United States, talked to people from the
4 PCAOB.

5 As you drill down through it, we believe the PCAOB
6 guidance is working, and we think that's ultimately where we
7 need to go.

8 I think to the extent you had two different

9 independent standards it would become very, very confusing
10 for the public, and so now I'd have, I'm independent here but
11 I'm not independent if you grow to a certain size, and it
12 just became -- it seemed like it was very confusing to get
13 to.

14 And I think for the most part what we're talking
15 about is the ability to implement standards, that I think
16 even smaller public companies can implement -- you know, once
17 they get the standard going and implemented, it's an easier
18 process for them to have something worked out, and I think
19 the PCAOB guidance does give the audit firms a lot of leeway
20 as to what they can and can't do.

21 Now, can we go as far as Dick wants, where the
22 auditors are going to do something for the client? I don't
23 think so. But we can't do that under AICPA standards very
24 much, either, so --

25 MR. JENSEN: I was thinking more along the lines of

1 allowing, and this is more along the lines of accessibility
2 to capital if you have an auditing firm who has been auditing
3 a company for three years following AICPA independence
4 guidelines, now the company wants to go public, now you have
5 to apply for those prior three years the SEC independence
6 guidelines, because they're now in a registration statement,
7 and whether there isn't a breakpoint there where it would be
8 okay for the auditor to follow AICPA rules until the

9 registration statement is filed.

10 MR. DENNIS: We talked a little bit about that, and
11 again kind of gotten to the point to the point that we find it
12 hard to believe that anybody wakes up tomorrow and decides to
13 go public, and so that there's at least some period of time
14 they have as an advance warning, and so they ought to be able
15 to get prepared for that, and so we --

16 MR. JENSEN: Well, I was thinking again --

17 MR. DENNIS: We didn't dismiss that, but --

18 MR. JENSEN: Yeah. We can maybe talk about this
19 off line.

20 But I feel like, especially with the SEC's up and
21 over rules, that in the private equity - venture capital
22 industry, it is very difficult for auditors to kind of
23 monitor their independence all the time in that world,
24 because you have to be sure you're independent for those
25 three years, which means you've got to look at an entire

1 portfolio of companies, what you're doing with them, and what
2 you're doing at the PEI level, and it's a conundrum.

3 I know that there's been some action trying to get
4 the SEC to maybe give a little more guidance in that area,
5 but it just seems to me it's a big issue with providing
6 services to companies that are private and then getting --
7 but trying to monitor them as if they were public. It's
8 quite difficult.

9 MR. DENNIS: I don't disagree.

10 MR. JENSEN: Okay.

11 MR. DENNIS: And that is something -- we can reopen
12 that in our committee discussions if the group would so
13 desire that we do that.

14 MR. JENSEN: Okay.

15 MR. WANDER: Any other comments besides Mark's?

16 Yes, Rich.

17 MR. BROUNSTEIN: Just to chime in and encourage you
18 to do that.

19 It seems like if we're not talking about creating a
20 new standard, we're talking about keeping the AICPA rules for
21 a larger level, right, for the smaller company, that seems to
22 me pretty harmless.

23 We don't have to recreate the rule, right. It
24 exists.

25 Anyway, just my two cents.

1 MR. WANDER: Any other observations?

2 (No response.)

3 MR. WANDER: All right. Thank you, Leroy and Pat,
4 and we'll turn to David.

5 MR. COOLIDGE: Dave Coolidge, Capital Formation
6 Committee.

7 Thank you.

8 We have a number of items that we've talked about

9 previously.

10 Let me give just a little color commentary, I
11 guess, into why we're focused on these issues.

12 First being ending the prohibition against general
13 solicitation and advertising for transactions.

14 With certain purchasers, this would be a private
15 placement, and what we're trying to create here is an
16 opportunity for private offerings to occur with certain types
17 of investors, obviously, wealthy, sophisticated investors,
18 where you wouldn't be running afoul of the private placement
19 rules by making it a broad solicitation, but only to this
20 group of people that would be able to take the risk, and
21 presumably, when the transaction closed, you would have a
22 very sophisticated and wealthy group of investors, and that
23 should be a decent standard not to -- if you achieve that,
24 that you shouldn't be penalized for having conducted an
25 offering that, you know, perhaps had a fairly broad

1 solicitation effort.

2 So that's a kind of an idea that we have that would
3 help certain companies in their private offerings.

4 I know this is a subcommittee or this is a
5 committee on public, smaller public companies, but to the
6 extent that the public markets are not available to someone
7 for whatever reason, that this opens up the private markets a
8 little more broadly for them.

9 Another issue is the issue of private placement
10 broker dealers.

11 The concept here is to again assist private
12 companies by creating a broader pool of people who can assist
13 them in raising capital.

14 The NASD registration process, as it currently
15 exists, is something that certain finders or brokers, you
16 know, find to be a little bit onerous, and the concept here I
17 believe is to create a, I don't know if I want to call it an
18 amnesty program, but a way of having a broader group of
19 people be qualified, go through a streamlined registration
20 process, and thereby be in a position to help smaller
21 companies.

22 Thirdly, private placement exemption adjustments.
23 I won't go into all the details here. I talked about a few
24 of them yesterday.

25 But the idea here again is to make private

1 placement activity more accessible for smaller companies,
2 easier to process and to succeed at.

3 We did have a fair amount of debate about the going
4 private or de-registration process, and I think we have come
5 up with a concept, when we talked about this yesterday, and
6 you mentioned the Ziegler situation, that they decided to
7 de-register but had an undertaking with their shareholders
8 that they would continue to provide them with information,

9 proxy statements, annual reports, a package of information
10 that investors would find acceptable.

11 In that particular case Bob Robotti said that
12 actually the stock traded up because the investors liked the
13 program.

14 Yes, they were going to de-register, but they were
15 going to continue to provide a nice information flow to
16 investors and they were going to eliminate an \$800,000 cost,
17 I believe was the number, so the stock went up on the basis
18 of that savings.

19 And we think that the idea here would be to have an
20 exemption from 13e-3 for micro-cap companies to de-register,
21 who were willing to provide -- were willing to, you know,
22 make a representation to their shareholders that they were
23 going to continue to provide information.

24 So that's a way of making it a little bit easier
25 for certain companies to de-register and save a lot of money,

1 but hopefully not harming investors in the process, maybe
2 benefitting investors.

3 Trading markets, we've talked about that
4 previously, our belief that the Bulletin Board market is an
5 important place and we want to make sure that someone is
6 encouraging the NASDAQ and the NASD in their arrangement now
7 where the NASD in fact is responsible for the Bulletin Board
8 but NASDAQ sort of runs it on a contract basis.

9 We want to make sure that, I think, someone at the
10 SEC take this on as a, I don't want to call it an oversight
11 responsibility, but a cheerleading responsibility to make
12 sure that that market is maintained and it's a good market
13 for companies that, you know, are not listed on one of the
14 major exchanges or on the NASDAQ as it's presently
15 constructed with listing standards.

16 Another one that we've talked about is 15-C-211
17 information, we want to make that public.

18 In conjunction with that, another ideas was put
19 forward with respect to compensation to broker dealers by
20 companies, and maybe we could have a chat about this.

21 I'm not sure how people around the table would
22 react, but the idea is, just like we've said, that it's hard
23 for small companies to get research analysts, it's hard for
24 small companies to get broker dealers to trade their stock,
25 and is there a way of allowing some company or corporate

1 compensation to broker dealers for providing the market
2 making service?

3 I'm not exactly sure what all the potential fallout
4 from that might be, but it was an idea that we have recently
5 raised.

6 Availability of Form S-3 available for Bulletin
7 Board securities.

8 I think what we want to recommend there is for

9 resale purposes it would be, the S-3 could be used for resale
10 purposes, not necessarily for registration purposes, and that
11 would be for Bulletin Board securities that meet the market
12 cap test that S-3 now applies to.

13 Debate on an issue with respect to national, or
14 NASDAQ small cap stocks -- this is a group of about 600
15 companies that are traded, they do meet listing requirements
16 -- and whether they should be deemed covered securities, in
17 other words, exempt from state review.

18 There's two points of view on this, and I'm not
19 exactly sure where we come out on it, but that would
20 obviously be a burden that you could take off of a group of
21 600 small cap companies that they presently have. When they
22 want to sell securities, they have to register with the
23 various states that require it.

24 Research is an area that we've had a lot of
25 discussion about trying to make sure that research is

1 encouraged and supported for small cap companies.

2 I think that we feel like we're in pretty good
3 shape there, that nothing that has come out of late or from
4 the SEC seems to indicate that they're doing anything to
5 discourage research or cut off payment flow for research.

6 It seems like, at least our sense is, that the
7 attitude at the SEC is to encourage this, allow company
8 sponsored research, continue the concept of soft dollar

9 payments for research.

10 So I think we're in pretty good shape there.

11 And then there's a technical issue, Rule 701, which
12 has to do with stock options,].

13 And we have a concept there that would allow stock
14 options to be granted and not be counted as securities
15 holders for the purpose of becoming a public company.

16 These would be what we call compensatory stock
17 options.

18 In other words, they're options to employees that
19 wouldn't trip a registration requirement by a company just
20 because they included too many people in their option pool.

21 And that is where I think we're in pretty much
22 alignment or agreement on most of these subjects.

23 I don't know if people around the table have issues
24 that are -- you know, they would take the other side of some
25 of these issues or have others that they'd like to add to the

1 list.

2 But that's kind of where we are, and we're getting
3 ready to, you know, come forward with pretty formal
4 recommendations on these.

5 Different subject. And I just want to, because
6 I've got the microphone, bring it up.

7 I'd love to hear before we leave what other
8 activities are going on out there with respect to

9 Sarbanes-Oxley reform.

10 The reason I ask this is I got a call from my
11 Congressman, Mark Kirk, who wanted me to come over to appear
12 at a forum to talk about Sarbanes-Oxley reform and revision,
13 and this was yesterday. He was holding a big session in
14 Chicago.

15 And so there are other movements afoot out there
16 other than this committee.

17 I'd like to think that this committee is going to
18 be in the vanguard and the most influential, but it sounds
19 like there's other people who are dealing with the same
20 subject and issue and taking the initiative on it, and I
21 don't know who is keeping track of everything that's going
22 on, but I think it would be interesting for us to know who
23 else is doing this stuff, and maybe, if possible, coordinate
24 with them so that they can have the benefit of all our
25 testimony and all our thinking and discussion and debate, and

1 try and get coordinated, as opposed to having five different
2 isolated efforts going on to address this subject.

3 MR. WANDER: Okay. Gerry?

4 MR. LAPORTE: I don't know what that particular
5 Congressman is doing. I know people on the Hill are --

6 MR. WANDER: This is Gerry Laporte, by the way.

7 MR. LAPORTE: Yeah, I'm sorry, this is Gerry
8 Laporte.

9 People on the Hill are actually listening to this
10 webcast today, I know, to try to coordinate their efforts
11 with our efforts, and we're in contact.

12 And as most of you know, the GAO is also doing a
13 study of Sarbanes-Oxley and small business, which we've
14 talked to and some members of the advisory committee here
15 have also spoken with the GAO, so we're trying to coordinate
16 their study with our study to make sure that, to the extent
17 possible, we're not bumping into each other.

18 MR. DENNIS: Gerry, do we know when the GAO is
19 going to issue their report?

20 MR. LAPORTE: Originally, I think there was a
21 December 2005 - January 2006 due date for that, but I'm not
22 sure whether that's still a good due date.

23 I think that they don't -- they're trying to figure
24 out whether it's -- I think whether they should ask for an
25 extension of that. I'm really not sure where that stands.

1 MR. WANDER: I actually talked to the people from
2 the GAO last week, and that's an accurate -- Gerry's is an
3 accurate statement.

4 But it will be around the same time that we're
5 going to at least go public with our recommendations.

6 As best I can tell, we've both been finding the
7 same information, and I don't know what their
8 recommendations, if any, will be.

9 So it's hard to tell. Yes.

10 I don't know of any other studies. People from the
11 Small Business Administration have been sitting in on these
12 meetings, and we've had contact with them, but I don't think
13 they're out making any recommendations as far as I know.

14 MR. LAPORTE: They did send a letter to Chairman
15 Cox, being very complimentary of this committee.

16 MR. WANDER: Well, why don't you circulate that?

17 MR. LAPORTE: I can see if the chairman is willing
18 to do that. I think that's a -- I think he probably would be
19 willing to do that.

20 MR. WANDER: Drew.

21 MR. CONNOLLY: Just two quick things.

22 Dave, since I was the proponent of the 15c2-11
23 broker compensation discussion, there really is a support in
24 the marketplace for this, and that is that the NASD
25 arbitrarily made a determination a number of years ago that

1 compensation for the due diligence work, not for making a
2 market, but for going through the sometimes arduous,
3 multi-back-and-forth tiered comments and questions, was not a
4 method to be compensated for, and that perhaps made sense
5 when the markets traded in eighths and quarters and the
6 compensation given to a market maker was a 30-day exclusive
7 to trade that security once it traded.

8 That 30-day exclusive is no longer relevant, and in

9 a decimalization world, there's literally no way for a broker
10 dealer to receive compensation adequate to cover the expenses
11 subject to the due diligence.

12 So the thought was, since they are regulated
13 entities responsible for their conduct across the board, that
14 they are no less deserving of due diligence compensation than
15 the attorneys or the accountants working with these public
16 companies, and I think Cromwell Coulson on the Pink Sheets
17 gave me a statistic that of the 400 15c2-11 submitting brokers,
18 market makers a couple of years ago, that number is now down
19 to 80.

20 So the other thing is that the prohibition is
21 regularly breached by back-door arrangements to compensate
22 the non-regulated entity the consulting firm or what have
23 you.

24 So I'd like to find a way to put an end to that
25 practice.

1 MR. WANDER: I do know the Ziegler people did
2 mention that, and they thought that was the reason why their
3 spreads increased, is because the brokers didn't get paid for
4 due diligence and keeping the stock listed the brokers had to
5 pay for and not the issuer, which is the big difference on
6 those markets.

7 So it's probably worthwhile to look at. I'm not
8 sure we ought to take on every issue in the world, because

9 having a rifle approach, I think at the end of the day we
10 will be far more effective on those big issues that I think
11 are really driving the marketplace.

12 But that is an issue --

13 MR. CONNOLLY: Of access to capital.

14 MR. WANDER: Yes.

15 Pat.

16 MR. BARRY: Dave, in your earlier agenda, you had
17 an item about adjusting the process for PIPE transactions. I
18 was just curious to see if you guys had discussed PIPEs and
19 what your thinking was there.

20 MR. COOLIDGE: Excuse me. Dave Coolidge.

21 We have discussed it. I guess we're welcoming
22 comments to improve the process, but I don't think that we --
23 the PIPE activity has been pretty significant, and if done
24 right, seems to be working for a lot of companies, and there
25 is an SEC issue, I think, with the conduct of certain

1 practitioners in the PIPE markets, and we think that's an
2 appropriate concern. Certain people are abusing information,
3 et cetera.

4 So we're going to just leave that in the SEC's
5 hands in the Enforcement Division, or wherever it falls, but
6 we think that the process is a valid one and it's a pretty
7 good one, and we're not really thinking about making a
8 recommendation in the area, but we're certainly open to

9 suggestions.

10 If people around the table that have had experience
11 feel that the process can be improved by adjusting some rule,
12 we're more than open to it, because we think it's a good
13 process, we think it's something that, you know, is providing
14 capital for lots of small companies that are public, and if
15 there's a way of improving it or streamlining it, we'd be
16 happy to listen, but we didn't come up with anything that we
17 were too upset about as it currently is being done.

18 MR. WANDER: And it's not just small companies. I
19 think if you look at the list that Drew passed out, you'll
20 see that there are some sizable offerings.

21 MR. COOLIDGE: Yeah.

22 MR. WANDER: Yes. Richie and then Rick.

23 MR. LEISNER: Richie Leisner.

24 Just a footnote -- the recommendation that we've
25 had on the list about the private placement broker dealer

1 registration.

2 I think Jerry Niesar mentioned this. He was the
3 ABA representative in San Francisco.

4 This is a proposal that's been around for a long
5 time, and it involves, if it's to be done successfully,
6 several different agencies.

7 And so our request, when it gets done up finally,
8 would be a request and recommendation that the SEC step out

9 in front and head a multi-agency effort in this regard.

10 Otherwise, this is -- we are afraid this will just
11 stay as a recommendation that will be around for even a
12 little bit longer, and no one is willing to get to the head
13 of the parade and start the process.

14 MR. WANDER: Rick.

15 MR. BROUNSTEIN: I have three comments now, so I
16 got a new one here.

17 The comment I would make on PIPEs, just to finish
18 that off, is if you've looked at all at integration rules.

19 Having done a lot of PIPEs, we get caught up in
20 those all the time.

21 There seems to be, you know, the strict
22 interpretation and what is really, you know, the SEC going to
23 look at or not look at, and it seems to me they can be
24 awfully limiting if taken to their extreme, you know, from
25 six month, you know, safe harbor rules to, you know, can you

1 close one out and do another one and should you be able to,
2 and oftentimes you can, but strictly you can't.

3 So I guess I would say that's an area that -- do
4 you want to comment on that, and then I'll go on to my other
5 questions.

6 MR. COOLIDGE: One of the private placement -- one
7 of the safe harbor issues that we are going to recommend is
8 shortening that six month period down to 30 or 60 days.

9 MR. BROUNSTEIN: Okay. That should help.

10 The other -- so a question on the S-3 and then a
11 comment on the de-registration.

12 But on the S-3, are you basically saying shelf
13 registrations are being excluded but the other kind of
14 registrations are okay, or are you more limiting than that?

15 MR. COOLIDGE: I think our recommendation is going
16 to say Form S-3 -- now, this is only for Bulletin Board
17 companies that meet the market cap test -- Form S-3 is
18 available for resale purposes.

19 Is that the question, or are you asking another
20 question?

21 MR. BROUNSTEIN: I thought the talk around here
22 seemed to be to broaden the use of the S-3, right, because
23 the big advantages are you can incorporate by reference and
24 then once it's out there, you don't have to update it every
25 time you do an annual audit.

1 And so it seems to me, other than maybe, you know,
2 I can understand why you wouldn't want to -- if you don't
3 have the market cap to do a shelf registration, that's, you
4 know, to pre-register shares, but otherwise, I guess if
5 you're excluding some, I'm wondering why you would exclude
6 them.

7 MR. LEISNER: We may need to get Gerry to jump in
8 here on -- this is Richie Leisner -- to get Gerry to jump in

9 on the technicalities here.

10 But I believe that S-3 is only available to NASDAQ
11 or exchange listed companies on a resale basis, and so --
12 which would have made sense, because when the rule was
13 propounded, you didn't have to be 34 Act registered to be on
14 the Bulletin Board, which you now do. So it's sort of a
15 technical expansion.

16 My recollection is that there's no float
17 requirement to use S-3 for resale purposes, just that you
18 have to be a 34 Act reporting company, and now you've got to
19 be on some part of NASDAQ.

20 So the thought would be, since Bulletin Board
21 companies have to be 34 Act filers, that it would be
22 reasonable to look at expanding the availability of S-3 as a
23 resale device.

24 My recollection is also that on the primary side,
25 it's just a float test and you don't have to be on -- I could

1 be wrong.

2 I'm looking at Kevin O'Neill on the other side of
3 the room here, and he'll let me know if I'm wrong, or Gerry
4 will.

5 But those are two sort of technical issues, the
6 idea being, to go back into English, the idea being to make
7 S-3 more available to more companies.

8 MR. BROUNSTEIN: Okay, so if you can carry that

9 thought, the way we're heading now with some of the
10 discussion here, with some corporate governance rules that
11 would affect the Pink Sheet companies, some minimum standards
12 for the micro-caps, whether they trade on the Pink Sheets or
13 the Bulletin Board, if they meet those standards, then they
14 ought to be entitled to take advantage of today's Internet
15 world and incorporate by reference, rather than exclude.

16 In other words, if we're going to put on
17 requirements on the Pink Sheets, then they ought to have the
18 advantages and not have to onerously file some document.

19 Really, the only difference is you're pasting
20 everything into one document and having to update it once a
21 year.

22 MR. LEISNER: Richie Leisner again.

23 Right, Rick, except when somebody says, "Oh, all
24 you have to do is X," if you can use the incorporation by
25 reference, of course, it is a far less costly undertaking.

1 Yeah, we hadn't seen any of that information, and
2 we were focused on this one narrow issue.

3 The rationale of it would be if there were -- if
4 the appropriate information were out in the marketplace and
5 it was accessible to the investing public, it certainly would
6 be logical to think about making incorporation by reference
7 available, which is what you could do using an S-3.

8 MR. BROUNSTEIN: So you make, yeah, so it may make

9 sense to, rather than simply define Bulletin Board, define
10 those requirements so that whatever we come out here, if we
11 broaden those requirements and that is accepted, then they
12 would fall in.

13 Then my last question on de-registration maybe
14 comes around to a similar point.

15 I'm not sure where that extra 800,000 we were
16 talking about in the example is now, but, you know, we're
17 talking about a system for the smaller companies, the
18 micro-caps, that is going to require them to do some,
19 depending on what we find out here as a committee on cost
20 effective, maybe some attestation to, or assertion to 404,
21 clearly some auditor independence in whistleblowing, I would
22 think that, you know, and we're talking about maybe resizing
23 the beneficial shareholders to try to catch people who are
24 today going dark on us.

25 It would seem like we should determine as a -- you

1 know, put our committees together as a group and decide what
2 are the minimum standards that make sense for these smallest
3 of companies, and not allow them to get out for, you know,
4 some other reason, like as I understood your de-registration,
5 you're saying they would have to apply certain financial
6 statements, but we're suggesting that they need more than
7 just to file audited financial statements, that they're
8 going to have to do a few other not necessarily onerous

9 things, but a few other things that would give some
10 visibility to those shareholders.

11 MR. CONNOLLY: Can I respond?

12 MR. WANDER: Let me see if I understand it, and
13 then you can.

14 What you are suggesting this afternoon is that if
15 you still -- if you're not buying out the public
16 shareholders, which Bob has some question about, there would
17 be, if you made a commitment to continue to flow information
18 to investors, whatever that package is, that there would be
19 an easier way to do that.

20 But I take it you're not suggesting any sort of
21 rules where there's in fact a squeeze-out of the
22 shareholders?

23 MR. COOLIDGE: Correct.

24 MR. WANDER: Okay.

25 MR. COOLIDGE: This is a de-registration this is

1 not a buyout. This is to give smaller companies a way of
2 ridding themselves of these onerous costs.

3 Now, maybe we're going to find out 9,000 other ways
4 to rid them of these onerous costs, but 13e-3, I think
5 that's the right -- yeah -- which is the de-registration
6 regime that currently exists, is a very expensive -- I
7 thought we in our committee talked about \$1 million or
8 something to go through that.

9 And people just say, "Well, you know, I'm trying to
10 save money, but you tell me I got to spend all this money to
11 save this money, it doesn't make any sense." So if they want
12 to save the money, go through the process without filing that
13 form, but make an undertaking to continue to supply
14 information to shareholders.

15 And obviously they, at that point, they
16 de-register. If they are on the Bulletin Board, they go off,
17 they wind up in the Pink Sheets where de-registered
18 securities do trade.

19 MR. BROUNSTEIN: So these are people that have
20 below the minimum requirements, so they --

21 MR. COOLIDGE: Whatever they may be --

22 MR. BROUNSTEIN: And they may change. But today
23 that would be 300 shareholders and \$10 million in assets?

24 MR. LEISNER: No. No, because those people under
25 the current -- Richie Leisner again.

1 If you fall below 300 stockholders, you can leave
2 the system with a free pass, just by filing a notice. That's
3 in the current law today.

4 We're talking about somebody who is not at 300
5 stockholders and doesn't want to game the system to get down
6 to 300 stockholders, and doesn't want to go through a 13e-3
7 transaction where they have a buyout.

8 This is somebody who says, "I'd like to go," and it

9 would be the standards -- it would be in the micro-cap world.
10 We would not be talking about, you know, a Fortune 100
11 company that would do this.

12 And so they would be -- they would undertake to
13 provide this information package, and then they could --

14 MR. BROUNSTEIN: Stop filing with the SEC?

15 MR. LEISNER: Yeah.

16 MR. WANDER: I think that's a point that didn't
17 come through, that you were going to enlarge the ability to,
18 in effect, go through the 15(d), whatever the form --

19 MR. LEISNER: Whatever the heck it is, yes.

20 MR. WANDER: The form that you file. Okay. I
21 think I understand now. Okay.

22 MR. BROUNSTEIN: So it seems like that's the
23 opposite of what these two committees, Corporate Governance
24 and 404, are talking about.

25 We're trying to widen the base, make it reasonable,

1 make it cost effective for these guys, but have more
2 transparency for companies that have, you know, enough
3 shareholders to be considered public, you know, and -- or not
4 allow them to trade at all.

5 In other words --

6 MR. COOLIDGE: Maybe if this is the only one we get
7 through, this is the way out for everybody. If we fail, then
8 all other --

9 (Laughter.)

10 MR. WANDER: Drew, and then Bob.

11 MR. CONNOLLY: Drew Connolly.

12 Very quickly, Pat, to the discussion about PIPEs,
13 we basically eliminated it, but I do recall there was some
14 testimony in San Francisco, and it has been in the Small
15 Business Forum.

16 The only issue, and I don't think it's one that
17 necessarily rises to a full recommendation level, is somehow
18 internally, and this is the entire form filing and review
19 process within the Commission, we were assured yesterday that
20 basically these documents come in and get examined in
21 relatively quick order.

22 I guess there's been some concern about the
23 turn-around time, and I think you have -- your firm has
24 recently gone through a PIPE or going through one?

25 MR. BARRY: My issue was just more of a general

1 question in terms of timing --

2 MR. CONNOLLY: And the other thing is, the timing
3 is perfect, because I expect to be at one of these two days.

4 Starting tomorrow at the Waldorf in New York there
5 is the annual PIPEs conference, and some of the largest law
6 firms in the country, and certainly some of the major broker
7 dealers and over 100 companies that are involved in the PIPE
8 marketplace, the hedge funds, and those folks will be in

9 attendance, so I might actually know more about this subject
10 when we get there.

11 Richie -- not Richie -- Rick, the issues
12 surrounding, and I take your point very well. We are
13 actually looking for the potential escape clause, which we
14 also hope, based on the other subcommittee's work, not many
15 people will feel -- not many companies will feel they need to
16 avail themselves of that out.

17 But it's also true that the president of the pink
18 sheets, Cromwell Coulson, has testified to us and very much
19 aware that he is working every day to expand the quality of
20 both disclosure and required information distribution on the
21 pink sheets.

22 So it would make sense to me -- I take your point
23 very strongly that the covered securities issues be extended
24 from the bulletin board to potentially his top tier. And
25 this -- I'm not asking for the SEC to work hand in glove with

1 a private company.

2 But if his top tier as described to me is reporting
3 companies who are doing what's determined here to be all of
4 the material requirements to meet these tests, and that is
5 his top tier within the pink sheets, I think that may blur
6 somewhat the distinction between the bulletin board and the
7 pink sheets, and the net impact of what we've done here
8 defining microcaps may very well create some level of

9 investor or speculator respectability that is heretofore not
10 available through pink sheet securities.

11 They are often spoken of in the same sentence as
12 fraud. Penny stock fraud, pink sheet. And I'm trying to
13 work very hard, as you may imagine, to decouple those terms.
14 Because it's very clear to me that there are hundreds and
15 hundreds and hundreds of little companies who don't meet the
16 fraud test but are in fact penny stocks.

17 The only final remark I have is that I know that
18 we've taken testimony and I'd like to thank our co-chairs for
19 really giving an expanded vision of the marketplace out there
20 and working very hard to bring balance to opposing points of
21 view. And I can think of no better than the comment letters
22 that we received this round where I guess perhaps predictably
23 but also very interestingly, the AFL-CIO weighed in on one
24 side of exemptive relief, and the U.S. Chamber of Commerce
25 weighed in on exactly the opposite sides.

1 So I found that revealing. But the one element of
2 testimony I don't think we've received or had access or
3 visibility to would be regulators. We've had no testimony,
4 despite the efforts within the subcommittee here of probably
5 one of the best securities regulators I've ever run into from
6 the state of Nebraska, we've had no testimony from the area.

7 And I know from a capital formation standpoint,
8 most of what we come up against is obviously the gentlemen,

9 ladies and gentlemen of corporate finance who are both our
10 hopes and the progenitors of this committee, but we're
11 running up against virtually in many of our recommendations,
12 certainly the finders, private placement, broker-dealer
13 recommendations and certainly some of the trading practice
14 recommendations, right smack up against the purview of the
15 Division of Market Regulation here within the SEC.

16 And my hope would be that we would be able to
17 elicit both some of their positions and some cooperation from
18 them in helping us do our mission.

19 Additionally, it would be insightful I think to be
20 given -- we bandy around a lot of statistics about the amount
21 of and the number of complaints in microcap fraud. I'd love
22 to hear somebody from the Enforcement Division give us some
23 overview of what that experience really is and what the
24 magnitude of those problems really are.

25 So that constitutes my comment.

1 MR. WANDER: Okay. Bob?

2 MR. ROBOTTI: I guess I had a couple of questions,
3 because when you described the going private transaction. It
4 seems to me of course today a company would only file a
5 13E-3 if they were going to do a reverse split, or if they
6 were doing a tender offer and it was in conjunction with
7 that.

8 If you had, you know, the idea of eliminating the

9 need to file the 13(e) kind of makes a lot of sense to me I
10 think, especially if, you know, the quid pro is we're going
11 to give you information on a go forward basis and therefore
12 provide data to shareholders and information.

13 The other potential requirement that you'd really
14 have I think would be a prohibition on the part of the
15 company that there's no plans to proceed with a going private
16 transaction within at least some, you know, a three-year
17 period. Because otherwise, you could potentially have
18 someone who files, provides information, you know, nine
19 months later therefore proceeds with a going private
20 transaction, which would have been subject to a 13E-3
21 filing, and potentially was even part of a plan or device
22 that came apart in pieces but not in total.

23 So, you know, to give those two things -- and I
24 think you give protection, shareholders protection
25 information and, you know, some kind of safeguard.

1 But I guess I didn't get the full context of what
2 you were saying. So what you're proposing to do would be to
3 broaden who would be eligible for deregistration through that
4 process, you know, beyond the 300 shareholder count?

5 MR. LEISNER: 13e-3, right.

6 MR. WANDER: Any other, Steve?

7 MR. BOCHNER: I've got a couple of comments. I
8 think the first is to get a bit more granular on this general

9 solicitation prohibition. You know, the 33 act is
10 constructed so that you've got, if you're going to solicit
11 generally, you've got to file a registration statement for
12 the most part. If you're not going to solicit, if you're
13 going to rely on a private placement exemption, that
14 purchasers need to be accredited. You need to have -- in
15 general need to not solicit generally.

16 And I guess I'm having trouble with the idea that
17 we would allow a -- let's say a private company that isn't
18 making information widely available, to generally solicit out
19 there and then have a purchaser come in and, what, merely by
20 signing an attestation that they meet certain accreditation
21 standards or net worth standards be able to invest.

22 And I'm wondering really how salable that is here
23 at the SEC, this idea of limiting general prohibition without
24 some checks and balances as to who those purchasers are, how
25 they get qualified. Is there any contours around this idea

1 of eliminating general solicitation that you can help me
2 with?

3 MR. LEISNER: Richie Leisner. Yes. You sound like
4 the same people who said when Regulation D was propounded,
5 which did away with offeree suitability, that that was the
6 biggest scandal since the sale of the Brooklyn Bridge as a
7 stock interest.

8 This is a bold suggestion. But there are places in

9 the securities laws right now under the exemptive structure
10 where you can have all the general solicitation you can
11 handle, like in Rule 144A, for example.

12 MR. WANDER: Subject to protections about
13 private --

14 MR. LEISNER: Well, yeah. But it's not that
15 there's -- so when you say granular, we have had some
16 discussions with senior staff personnel about how we would --
17 and we need some more discussions -- to decide what those
18 qualifications would be in terms of wealth, sophistication or
19 relationship to the issuer, sort of those three general
20 categories.

21 But I think those things are all doable. I think
22 that there's a lot of, you know, at the one end of the
23 spectrum, some people would say, oh, we already have that
24 definition. We call them accredited investors. And at the
25 other end of the spectrum, people say, well, no, that's no

1 good. Maybe they should be QUIBS, you know, Qualified
2 Institutional Buyers or something much, much, much, much
3 higher.

4 There's a big gulf in between there that we need to
5 talk about. And the issue about qualifying would be equally
6 applicable to accredited investors now. Some guy comes in
7 off the street. He says I'm a millionaire. He checks the
8 box, and you have a private placement. And that was a

9 scandalous thought 20 years ago or a little more than 20
10 years ago, but it seems to work pretty well.

11 And I think working with the regulators, we could
12 come up with -- I hope we could come up with a construct that
13 would be bold in response to what Herb and Jim asked us to
14 do. We have some work to do in that area.

15 MR. BOCHNER: Yeah. I don't mean to sound like the
16 detractors. I'm actually a fan of Reg D, and I think the
17 balance there is appropriate. I think it's different,
18 though, when we're going to solicit generally. I mean, if
19 we're really talking about reaching out there into the TVs
20 and newspapers with private, you know, advertisements focused
21 on people who -- and the recipients are going to be people
22 who are not accredited, I really do think you've got to think
23 long and hard about the protections there.

24 I mean, I think it worries me that coming out of
25 this committee we would sort of open up general solicitation

1 without making sure that there were checks and balances that
2 ensured that people who ultimately invested really were
3 people who could fend for themselves and didn't need the 34
4 Act information. So maybe I'll just let you guys debate this
5 fully and --

6 MR. LEISNER: Well, no, that's a terrific concern,
7 but it's just a challenge to the people who sit down and do
8 the detail work. The question is whether you're willing to

9 sit down at the table and talk about the concepts with an
10 open mind. All of those concerns are perfectly legitimate.

11 MR. BOCHNER: Okay. All right. I was just trying
12 to get behind -- I wasn't -- I didn't want to throw cold
13 water on it, too much cold water, but I just wanted to
14 understand whether there was some thinking about the details,
15 and maybe I'll just hold off till you guys --

16 MR. LEISNER: Well, Steve, I think that's -- but I
17 think that's very useful, because there's going to be --
18 there's going to be pushback. We might as well -- we expect
19 it, and you're -- I think you may be out of water balloon
20 distance on the other side of the room.

21 (Laughter.)

22 MR. BOCHNER: All right.

23 MR. LEISNER: But it's a perfect -- that's a
24 question we welcome, and we just have to get to the details
25 of it all. And initial discussions with the staff were I

1 think were encouraging, that this is a matter that we could
2 discuss and talk about and try to come up with some
3 parameters.

4 Obviously, from the one side, if the financial
5 qualifications are such that, you know, you only need -- such
6 that you got to be worth a jillion dollars to qualify, that's
7 not going to be so terrific. And we'll have to talk about
8 the means by which you do stuff.

9 MR. WANDER: So the devil is in the details.

10 MR. LEISNER: Thank you, Mr. Chairman.

11 MR. BOCHNER: Okay. Good. Well, I'll agree with
12 him on that and look forward to hearing that --

13 MR. WANDER: And without the details, it's hard to
14 sort of set the parameters. And it's also hard till you see
15 the whole construct.

16 MR. BOCHNER: Yeah. I mean, for example, a
17 marketplace with checks and balances where the people that
18 came into it were prequalified somehow, and then you could
19 solicit generally into that. I mean, that kind of an idea
20 makes sense to me, but.

21 All right. We'll look forward to that. The other
22 thing I wanted to comment on was the NASDAQ, the discussion
23 concerning the NASDAQ small cap exemption from the blue sky
24 laws. And today if you're a NASDAQ national market because
25 of the National Securities Market Improvement Act, you don't

1 have to comply with the state blue sky laws. Those laws have
2 been preempted.

3 The NASDAQ small cap companies have the same
4 governance standards. They file reports with the SEC. These
5 are smaller companies, and yet I have a hard time seeing what
6 value it is to make those companies simply because their
7 market cap isn't 75 million, it's 50 million or their trading
8 price, you know, is at a different level, why those companies

9 ought to pay when they're doing securities offerings the
10 state blue sky registration fees, and the larger companies, by
11 virtue of their somewhat higher market caps, should not.

12 So I guess where I come out in the balancing is
13 this is an opportunity for us to reduce costs of smaller
14 public companies, in my view, and I think Jack's probably
15 going to disagree with me here, but in my view, I think we
16 can do that without impairing investor protection, and I'd
17 like to see some evidence that the absence of blue sky
18 registration at the NASDAQ national market level has created
19 some problems, or similarly, that the existence of that state
20 regulation, that duplicative level of state regulation, in
21 addition to the federal regulation, has helped somehow.

22 So I would encourage you to continue down that path
23 and evaluate whether or not NASDAQ small cap ought to be
24 treated as a covered security, and we should encourage the
25 SEC to take some steps in that direction.

1 MR. WANDER: Jack?

2 MR. HERSTEIN: Jack Herstein. I'll disagree to
3 disagree with you. You mentioned NISMEA back in 1995. I
4 think at that time most states already gave NASDAQ the same
5 exemption they give the American Stock Exchange and the New
6 York Stock Exchange.

7 The problem is now there's two tiers to the NMS.
8 You have -- or two tiers to NASDAQ. You have the NMS, which

9 is your upper level companies, which is about, what, 3300, I
10 believe. Then you have the small cap companies, which is
11 about 578 right now.

12 The problem is the listing standards. You have
13 corporate governance for both at the same, and they have been
14 the same. The problem is that listing standards,
15 stockholders equity, price per share, well, basically every
16 listing standard is somewhat different on the small cap
17 compared to the NMS.

18 Now you have the listing standards for the New York
19 Stock Exchange, which are greater than the NMS. Then you
20 also have the listing standards for the American Stock
21 Exchange, which are lower than the NMS. The problem that the
22 states have, at least that I would have, is that if you give
23 the small caps the same exemption that you do with the NMS
24 companies, what will AMEX do, and will the small caps then
25 still drop their listing standards?

1 You know, because the listing standards have been
2 dropped over the years.

3 MR. BOCHNER: Well, I mean, there's always a risk,
4 you know, I suppose there's a theoretical risk NMS will drop
5 their listing standards, but they're not, you know, I think
6 those governance thresholds, board independence, you know,
7 all of those reforms apply to small cap companies.

8 I think the only thing that's different today, and,

9 you know, they have to comply with the 34 Act, so the only
10 thing that's different is the size. And so I guess my
11 question is, and maybe this is sort of an evidentiary thing
12 that we ought to ask for more information, but what is it
13 about size that suggests that we ought to have this
14 additional layer of state regulation, which is an added cost
15 to these companies that are least in the position to afford
16 it? So this seems squarely in the mandate of our committee,
17 which is finding ways to reduce costs and not impair investor
18 protection.

19 So I want to -- I think the reducing costs issue is
20 self-evident. Then the question is, how are we impairing
21 investor protection if we do this? And I guess that piece of
22 it isn't obvious to me that somehow this would create a
23 problem.

24 MR. HERSTEIN: I don't disagree the cost -- the
25 cost is not that great. There would be a cost savings. The

1 problem is, you know, I'll flip it the other way, name one
2 small cap company that the states have stopped from
3 registering again. I don't believe -- I don't think I've
4 seen a small cap company registered in Nebraska in the last
5 18 months.

6 Now either they're bypassing Nebraska, which I
7 would doubt, or they're just not making the IPO or the
8 listing filings in the states. But I guess I have not heard

9 like years ago how the states were hindering capital
10 development, capital formation, don't hear those arguments
11 any more. So I guess if I'm wrong on that, let me know.

12 But also -- one more thing. I do agree with your
13 previous comment on the private capital. It is bold. I will
14 agree with that.

15 (Laughter.)

16 MR. WANDER: Rick?

17 MR. BROUNSTEIN: Just to weigh in on blue sky, I
18 mean, I agree with Steve. It's -- first of all, the AMEX
19 standards are lower than the NASDAQ small cap standards, and
20 you have the exemption. It seems to me where we're heading,
21 we just need to converge on some of these things, to talk
22 about who should be eligible for an S-3, that with the new
23 standards we're talking about coming out of corporate
24 governance and coming out of the 404 committee on minimum
25 transparency that these companies have, that we ought to --

1 these other things that were sort of safeguards, and I'm not
2 sure why blue sky law was a safeguard at all, but assuming it
3 was, it seems to me we've now replaced it, and so we
4 shouldn't -- we ought to be converging around some of these
5 definitions.

6 And if you're -- you know, we're kicking around the
7 S-3. If you're eligible to do that whether you're on the
8 bulletin board or the pink sheets or you're at a certain

9 level and you have to meet certain corporate governance and
10 404 standards then, you know, you shouldn't have to do all
11 this other, you know, stuff. My opinion.

12 MR. WANDER: Okay. Further comments? Questions?

13 MR. CONNOLLY: Mr. Chairman, in speaking to the
14 mandate we were given in the beginning of our committee to
15 oversee or to look at the totality of federal securities
16 regulations, not just Sarbanes-Oxley, a large component of
17 the microcap community that I speak to continues to be deeply
18 disturbed at both the implementation and some of the elements
19 of regulation SHO.

20 The continued maintenance of threshold lists which,
21 by regulation are supposed to be self-collapsing by having
22 them regularized out, versus the fact that on many of these
23 securities, from Martha Stewart OmniMedia to Overstock, to
24 name, I guess, the two most famous ones, or the ones most
25 often talked about, those open short fails to deliver have

1 existed in excess of 100 days, and the regs call for 13.

2 So this is a capital formation problem.

3 Obviously, with open shorts and fails to deliver
4 and the possibility of naked short selling beyond the
5 outstanding issued, it makes it incredibly difficult to raise
6 capital if you're in the toilet of market cap as a result of
7 being put there by an aggressive either on-shore or
8 off-shore, whatever the net implications of how you got there

9 by having a short selling problem.

10 I'd just like us to think about possibly
11 encouraging the SEC to reaffirm that 13-day solution in
12 Regulation SHO, and then I'd probably question, I don't
13 know if we're going to, but why excesses of the past were
14 grandfathered into SHO and not, you know, open on a case by
15 case basis to further examination and enforcement.

16 MR. WANDER: Okay.

17 We did receive a lot of comments on our
18 questionnaire about short sellers.

19 I must tell you, unfortunately, I'm not a short
20 seller expert, but we'll see if we can look into that.

21 Any other questions, comments?

22 It's now about 2:25.

23 If there aren't any, I think -- yes, Mark.

24 MR. JENSEN: I have one.

25 You were so close to escaping.

1 This is actually really quick, and it's for Gerry.

2 MR. WANDER: No, no.

3 I'm going to next turn --

4 MR. JENSEN: Oh, you've got --

5 MR. WANDER: -- go to another meeting. Next steps.

6 MR. JENSEN: Okay.

7 This is for Gerry.

8 The comment letters on internal control and the

9 Commission's rules on internal control are due on the 31st.

10 Can we get copies of those letters, at least in the
11 404 Subcommittee, at some point?

12 MR. LAPORTE: Yeah. They are available on the
13 Internet --

14 MR. JENSEN: They are?

15 MR. LAPORTE: As they come in, they're posted on
16 the Internet.

17 MR. JENSEN: Oh, okay.

18 MR. LAPORTE: So you can just go to the release
19 number on the SEC's web site, and it should have an icon
20 there, link that you can -- it should say, "Comments on this
21 release are available."

22 MR. JENSEN: Okay.

23 MR. LAPORTE: You click on that, and you can
24 printout whichever ones you want.

25 MR. JENSEN: Because I think those comments will be

1 important for our subcommittee.

2 Thanks.

3 MR. WANDER: This is an announcement.

4 Don Nicolaisen's farewell reception is in this room
5 at 4 o'clock today, and all of you who are going to still be
6 in Washington are more than welcome to attend, and I'm sure
7 Don would like to see all of you at that time.

8 So those who have the time availability, please

9 attend.

10 I think Jim and I would like to move on to, really,
11 next steps, which I think we made a lot of progress today.

12 I think the discussion with the full committee
13 being presented with each of the subcommittees'
14 recommendations or observations so far to date and having the
15 comments, I think is a good start to finalizing our
16 recommendations.

17 And we've probably slipped a month in the basic
18 calendar that we had established, and I think that what we
19 have to do to sort of catch up or catch up is to schedule
20 another meeting here in Washington, the week of December
21 12th.

22 I know that it's difficult. People already have
23 items on your calendar.

24 But I don't, Jim and I don't know really any other
25 way to address this issue, other than getting together, and

1 that means having the subcommittee recommendations to us
2 before then.

3 I did check -- Janet, unfortunately, has left, but
4 I did check with Kurt and Rick, and I think you should be on
5 target to get us something for that date if I read you both
6 right.

7 So it's the week of the 12th. I don't know -- the
8 14th or the 15th are the days, I think, right, Jim, that we

9 could get this room probably and meet again.

10 Is there any strong preference for one or another
11 of those dates?

12 Yes, Pastora.

13 MS. CAFFERTY: I have a board meeting on the 15th.
14 I could -- and the 14th. I can cancel the 14th, I can't
15 cancel the 15th.

16 A PARTICIPANT: This will be a one-day meeting?

17 MR. WANDER: One-day meeting.

18 A PARTICIPANT: What's the day of the week?

19 MR. WANDER: Wednesday is the 14th.

20 A PARTICIPANT: The 14th is my vote.

21 MR. WANDER: All right, 14th it is.

22 Going once, going twice -- fine.

23 We probably will make telephone arrangements for
24 those of you who couldn't make it, but I hesitate to say that
25 because it's so much more valuable to have everybody in the

1 same room to discuss these issues.

2 So what we would like to do is have subcommittee
3 recommendations delivered to Jim and I and then we'll package
4 the whole package and get it out to everybody beforehand.

5 We are going to start drafting some of the portions
6 of our report in any event, which will be essentially
7 introductory paragraphs, et cetera.

8 And the recommendations have to be in enough detail

9 so that you don't have to ask questions about what you're
10 going to do.

11 I don't think you have to get rule language or, you
12 know, draft it as a rule, but I do think it should answer the
13 questions about how it would be applied, et cetera.

14 Yes, Rick.

15 MR. BROUNSTEIN: So are we going to use a format
16 similar to what you did on the Size Committee, or are you
17 going to leave more discretion in there?

18 MR. WANDER: I'm not sure --

19 MR. DENNIS: Herb, maybe if you just get out some
20 guidance on how you want us to format these recommendations,
21 you know, like for the preparation of this committee was just
22 a very brief outline. My sense is you want something a
23 little more.

24 MR. WANDER: I think we want actually something
25 more like what you actually submitted two weeks ago.

1 But that's a good suggestion.

2 So you don't have to guess, we will get something
3 out to you.

4 MR. DENNIS: And then, Herb, could you --

5 MR. WANDER: What?

6 We'll get you format.

7 MR. DENNIS: And then timing, Herb, of when you
8 want those recommendations?

9 MR. WANDER: Well, if we have it the 14th, why
10 don't you try and get it to Jim and I the 7th or the 8th.
11 We'll try and get it to you before the weekend, so you'll
12 have the weekend to review it.

13 Does that make sense?

14 MR. SCHLEIN: And very specific --

15 MR. WANDER: Yeah, I think so. I think so.

16 I mean, if you're not specific, we have to do, you
17 know, "What did you mean and how is it going to apply," you
18 know, that means we have to go back to the drawing boards
19 again.

20 I find writing things down, then you read them and
21 then you see where the holes are and whether it works or not.

22 So that's the plan.

23 Any other comments, business?

24 MR. LEISNER: Could you walk us through the next
25 few months?

1 MR. WANDER: Then we will put together a whole
2 report, which we are going to meet January -- we have a
3 scheduled meeting.

4 We'll try and have to you -- then I think we've
5 caught up, Ted, to our regular schedule.

6 We're meeting on January 9th, review the whole
7 report up or down, and then it will be published for public
8 comment a week later in the Federal Register and on our web

9 page.

10 And then I think we're caught up on our schedule,
11 which would be send it out for -- is that right?

12 We'll send out the report the 29th, have a meeting
13 the 6th, publish it the 17th.

14 We will have public comment -- this is January,
15 January.

16 MR. BROUNSTEIN: The meeting --

17 MR. WANDER: January 9th. If I said the 6th, I
18 apologize.

19 Public comment will be for a month, and we will
20 review those public comments, respond to them, and have our,
21 essentially our final meeting March 20th, to adopt or reject
22 the plan.

23 MR. CONNOLLY: Why don't we have pictures taken
24 handing over the final book?

25 MR. WANDER: No. And in fact, I will say this,

1 that Chairman Cox thought that we might want to actually
2 present the report to the full Commission, rather than by
3 mail, live, so that we can not only present it in writing,
4 but describe it and answer any of the commissioners'
5 questions.

6 Rick.

7 MR. BROUNSTEIN: The rest of the meetings will be
8 here in D.C.?

9 MR. WANDER: Yes.

10 Now, I know your subcommittee might want to meet in
11 Chicago, and that's fine. That's fine. We have the
12 facilities for any meeting.

13 And I will follow up with you, Leroy, with Huron.

14 And we all have considerable work to do, although I
15 think we've come a long way in the past two days to move the
16 program along to a place where I at least feel comfortable.
17 Jim agrees.

18 Dick.

19 MR. JAFFEE: Dick Jaffee.

20 We talked about this yesterday, and just thinking
21 ahead on the report writing, that I agree that a preamble
22 which identifies issues and gives context to the
23 recommendations, if we could do it, would be important.

24 And then I think at the end, if there are such
25 things, we can perhaps have a look forward of emerging

1 issues, if we know if there are any.

2 And then, finally, the last thing, which I think is
3 the most difficult thing to do, it would always be nice, like
4 we do this in the company when we make a major investment or
5 a capital expenditure or something, to have some way of
6 looking back and saying, "Well, we did all this, now what's
7 -- you know, what happened?"

8 And somehow, it would be very nice if the SEC could

9 tell us, or somebody could tell us a few years into the
10 future about which of the recommendations were not only
11 adopted but what was the impact of it.

12 So I don't know. That's a much more difficult
13 thing to put down specifically, but it would be interesting.

14 MR. WANDER: No, I think that's a good idea, and I
15 do think the format will have, obviously, a preamble setting
16 the stage, and I do think issues that we think deserve
17 further attention should be mentioned, so that they're not
18 lost on people for the next advisory committee, or for the
19 Commission itself to address.

20 I think we're at a stage in the whole securities
21 law development where we're being forced, frankly, because of
22 the explosion in communications and Internet and everything
23 else, to really keep far more current and not have
24 regulations that are on the books 20 and 30 years without
25 some sort of sunset review as an automatic process.

1 With those parting remarks, any other comments, new
2 business, old business?

3 MR. CONNOLLY: Dick, I think we're going to be able
4 to find out the impact of our work by looking at the health
5 of the capital markets, particularly the tiers that we're
6 working very hard to preserve, protect, and enhance.

7 And I don't know if the metric is going to be the
8 number of additional public companies that are able to enter

9 the space because of our efforts or the market value of those
10 companies, whether they're graduating from the pinks to the
11 small cap.

12 I'm not sure about the metric we'll use, but we
13 will know if the impact is in the right direction, I suspect
14 by looking at the terrain.

15 MR. WANDER: Okay. I want to thank each member of
16 the committee for your really dedicated service and
17 participation, and look forward to continuing the progress.

18 Thanks. The meeting is adjourned, so those of you
19 on the Internet can turn it off.

20 (Whereupon, at 2:38 p.m., the meeting was
21 adjourned.)

22

23

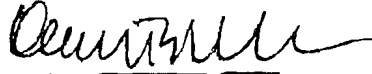
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CERTIFICATION

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



Herbert S. Wander
Committee Co-Chair

1/12/00

Date

Index of Written Statements Received

Listed below are the written statements received by the Advisory Committee between its meetings of October 14, 2005 and October 25, 2005 and the dates of receipt.

Oct. 25, 2005

Gerald G. Morgan, Jr., Burdett, Morgan, Willlamson & Boykin, LLP on behalf of Church Loans and Investments Trust

See also:

- * M. Kelly Archer
- * Jack R. Vincent
- * Steve Rogers
- * Bill R. McMorries
- * Michael A. Bahn
- * Larry G. Brown
- * Michael W. Borger
- * Alfred J. Smith

Oct. 21, 2005

A. John Knapp, Jr., President and CEO, ICO, Inc.

Oct. 17, 2005

Edmund M. Ruffin, Executive Vice President, Capital Formation Sector and Business Development, Biotechnology Industry Organization