UNITED STATES SECURITIES AND EXCHANGE COMMISSION

SEC SMALL BUSINESS CAPITAL FORMATION

ADVISORY COMMITTEE MEETING

Tuesday, August 13, 2019
9:36 a.m.

President's Fitzgerald Boardroom
4th Floor of the Mike and Josie Harper Center
Heider College of Business
Creighton University
602 N. 20th Street
Omaha, Nebraska
PARTICIPANTS:
1. Jay Clayton
2. Elad L. Roisman
3. Carla Garret
4. Jeffrey Solomon
5. Youngro Lee
6. Robert Fox
7. Sara Hanks
8. Brian Levey
9. Sapna Mehta
10. Catherine Mott
11. Jason Seats
12. Hank Torbert
13. Mark Sharma
14. Greg Dean
15. Martha Legg Miller
16. Julie Davis
17. William Hinman
18. Jennifer Zepralka
19. Jenny Riegel
20. Mike Pieciak - by phone

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2 Overview of Harmonization Concept
3 Release
4 SEC Proposal to Amend Financial Disclosure 
5 Requirements Relating to Acquisitions and Dispositions of Businesses - Panel One
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7 Commissioner Statements
8 SEC Proposal to Amend the Accelerated and Large Accelerated Filer Definitions - Panel Two
9 Caucus on Current Small Business Capital Formation Issues
10 Adjournment

PARTICIPANTS(CONT.)
1 PANEL ONE:
2. Matthew Swartz
3. Bill Korn

1 PANEL TWO:
2. Charles Crain
3. David Maley
4. Mike Raab

PROCEDINGS
1 CARLA GARRET: I would like to confirm who the members are -- for those of you on phones --
2 Thank you to Creighton University for hosting us here today. They have been gracious --
3 I would like to introduce --
4 We're going to wait for a name --
5 (The Committee waited for audio visual technical difficulties to be resolved.)
6 CARLA GARRET: Well, I don't need to call the meeting to order again because I've already done that,
7 and we've established that there is a forum. And so I wanted to thank Creighton for hosting us. They have been great and have been very gracious in everything that we're doing here today.
8 Here is a brief overview of the agenda items for today's meeting. In June the SEC requested public comment on ways to simplify, harmonize and improve the exempt offering framework to expand investment opportunities while maintaining appropriate investor protections and to promote capital formation. The harmonization release is quite comprehensive and large enough to take up multiple of our committee meetings.
9 And so today what we will be doing is focusing on developing a framework for this committee's work
recommendation on harmonization release.

Today we will also be discussing Regulation SX related to merger and acquisition disclosures plus accelerator filing definition. These two rules apply to public company disclosures and are timely because the SEC has just proposed an amendment to these two areas, and the public comment period has just ended.

As the SEC staff and Commissioners deliberate on how to move forward, the committee can provide perspective on how the proposals would impact small businesses. And what we are hoping today is if we can provide actually recommendations to the Commission on these two rules.

I would like to mention that for members of the Committee who don’t work — regularly work on public company reporting requirements, your perspectives on these issues are still very important and future committee meetings will likely have much more focus on private company and exempt offerings. Please note that Chairman Clayton — Clayton and Commissioner Purse will be joining later in the day, likely around lunchtime.

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Please note that Chairman Clayton — Clayton and Commissioner Purse (phonetics) will be going later in the day, likely around lunch time —

Now, I would like to introduce the SEC staff with us today. We have Martha Legg Miller who serves as the SEC advocate for small business capital formation and she is a member of the committee. Thanks, Martha.

And we have Julie Davis, senior special counsel in the SEC office of the advocate respondent of capital formation and has been incredibly instrumental in everything for today’s meeting so thank you very much.

Also we have Bill Himan, who is the director of the SEC business and corporate finance committee. Bill leads the division responsible for, among other things, drafting SEC rules and forms regarding the office security leading the rules —

The committee heard from Bill about recommendations of small businesses at the first meeting.

(Inaudible.)

If you have a point to add a question, please e-mail Julie, and Julie will relay them to us. Thank you.

I will start today with our first agenda item is SEC harmonization.

Since our May meeting — oh, I'm sorry, I —

I was in the middle of introducing Bill.

I'm sorry.

It's worth noting that Jennifer's policy office is different than Martha's advocacy office. Jennifer is with the policy office that takes relief in drafting the full release of the offering and to draft the harmonization concept relief. And as I was mentioning to those this morning, thank you very much. That it is why it is a relief, so thank you.

Thank you everybody for traveling to Omaha. Our first agenda item today is SEC harmonization law and relief. Since our May meeting the SEC has published a request for public comment on ways to simplify, harmonize and improve the offering framework.

The concept release provides a thorough overview of the current framework for exempt offerings, and requests comments on a broad list of issues.

Simultaneously the commission will release the staff report on the impact of Regulation Crowdfunding on capital formation and investor protection, looking back at three years since the effective date of Crowdfunding rules.
Before discussing how this committee wants to approach this opportunity to provide its strategic input, Bill and Jennifer will provide us an overview of the concept release and the harmonization effect.

Bill. Jennifer.

WILLIAM HINMAN: Sure. Thanks very much, Carla, and thanks from Core Fin to Creighton University hosting us today and Martha for organizing this, and I really want to thank the committee for coming to Omaha to provide input on these important rule makings.

The first one we were talking about is a concept release, the harmonization concept release, so in itself, it's not at the rule-making stage yet, we're really seeking input, and this committee's input will be incredibly valuable. The private placement market is significantly larger than the public offering. Last year I think it was about 2.9 trillion dollars raised in the private placement market versus 1.4 trillion in the public registry market. So it's an important space, and it's one that we hadn't really looked at in a very comprehensive way, and so this concept release is intending to do that and to get input on a whole host of issues, as Carla mentioned, particularly whether we can bring the rules together in a little bit more cohesive fashion.

Since 2012 we've been adding some private placement exemptions, the Jobs Act, added Crowdfunding, we've expanded Reg A, we've added Reg A plus, and then Reg A has been itself expanded for public companies to use as well. And as we've done that, we haven't sort of thought about how do these all fit together. One of the other things that we have looked at a little bit, but we haven't really done any real rule making on is the current definition of a credited investor. And that definition obviously plays a very important role in how our private placement exemptions work. The credit investor obviously is allowed to invest in a lot more wider range of private placement options without limitations, and we hadn't looked at that group to see if we have the right group there and are doing the right thing in terms of investor protection, as well as making something that's easy to work with and is useful in terms of capital formation.

Just so the committee knows, as we approach the harmonization release and thinking about what we can do in a very broad way to bring all that together, we will probably try to bite off the accredited investor definition first. Right now it's on our regulatory agenda for late in the year, and we expect to deal with that.

And I think that will actually make the harmonization exercise a little easier because then we'll know this is our group of accredited investors, or, you know, there's some good ideas out there around how to change that to broaden that some, to look at sophistication of investors a little bit more carefully than we have in the past. Numbers haven't been adjusted for a while, so we'll have an open mind in how to approach that field of potential investors, and we'll try to get that done before we tackle, okay, now that's that group of accredited investors, we also have unaccredited investors who participate in some of our private placement exemptions, let's make a rational field for them to both participate in. The chairman has really emphasized capital formation generally, and the smaller investor's access to private opportunities beginning -- you know, going back to where I began with the size of the relative markets. There's a number of interesting opportunities in the private space that if you're not an accredited investor today, you have very limited opportunity to engage in those opportunities. We are, and through the concept release, looking at is that appropriate, is there something we can do to facilitate the smaller investor having a more diverse range of options.

One of the things that Jennifer will talk about in a little bit more detail is that we've actually invited our colleagues and investment management to think about, you know, investment vehicles and how smaller investors may participate through an intermediary to get more access to some of these funds. Right now the universe of private funds and funds that engage in some of this 2.9 trillion market is somewhat limited to credit investors for a host of reasons, some of which are investment management division rules, and we want to work with them to think about as we change our rules is there something that could be done in the collective space to do what the chairman has suggested that we might want to be thinking about, which is making more opportunities available for more folks.

So that's something to have in mind as you're -- you're thinking about commenting here as well as, you know, the -- the credit investor point.

Jennifer has done a tremendous amount of work on the harmonization release. I just want to recognize that. I think -- we're at a Jesuit university, I think the theme is men and women built for others, and Jennifer was built for that release. I mean, she has done a fabulous job, and I really appreciate what she and her team has done there.
If you read it, and I congratulate you if you do, it's a long comprehensive basically treatise on what goes on in our private placement space. And with that, I'll let her speak more about that because she's the best informed person I know about about the topic.

Jennifer

JENNIFER ZEPRALKA: Thank you, Bill. Thanks very much. I need to give some credit back to the other members of my team who worked so hard on this release. Emara Slavens (phonetic) and Jenny Riegel. Jenny will be here later. They did a lot of the drafting all by themselves, so I want to thank them as well, not take all the credit for myself.

Just to talk a little bit more about what's in the concept release to launch your -- your discussion, it is a -- it is big -- a big document. And I hope you'll get a chance to read it, or at least read sections of it that you're most invested in, but it -- it broadly reviews all of the available exemptions for -- from the registration requirements of the securities laws that are used for capital raising. We -- we stayed away from most live the resale exemptions and the Rule 701 that we're focusing on capital formation here. It covers quite a bit of ground, and includes a lot of questions to explore whether there are overlapping exemptions that create confusion for issuers that are trying to figure out the most efficient way to raise capital, whether there are any gaps in the framework that might make it difficult, especially for smaller issuers to find the right exemption from registration, and we were asking a lot of questions about whether we've got the right exemptions for each stage of their business cycle. So, you know, does our framework work for anyone in the garage to on the verge of going public, and we want to look at concepts like integration to determine whether we can and should do more to allow issuers to transition from one type of exempt offering to the next, and ultimately to a registered public offering if that's what's appropriate for that company.

There are sections on each of the capital raising exemptions, so the private placement exemption in Section 482 of the Securities Act, Rule 506(b) and (c) of Regulation D, Regulation A, Regulation 50 -- or Rule 504 of Reg A, the Intrastate Offerings 147 and 147A, and Regulation Crowdfunding.

So as you flip through the release, you'll see there's a section on each of them, we give some background, we ask questions about how we can improve each of those exemptions. There's a -- the first section of the release talks bigger picture, general questions about how we can improve the framework across the board, and then it goes into those more specific questions about your exemptions. That discussion for each of them has been informed by a lot of feedback from the public, including prior advisory committees, prior forums, comments we've received, conversations with market participants. So a lot of the concerns that you may have are probably already sort of acknowledged in the release, but we'd love to hear your feedback on -- on what we can do about those issues.

For example, in the Regulation Crowdfunding section we ask a lot of questions about whether we should be doing something to the offering limit, whether we should be allowing special purpose vehicles to use the exemption, things that you know, have been coming up over and over again.

In the Rule 506 section we talked about verification of accredited investor status and whether there's anything that could be improved there that would make that exemption more attractive, whether additional clarity is needed around the idea of what -- what is general solicitation, that sort of thing. So too many questions to go through here, but as -- if you -- if there are sections you're particularly interested in, I would recommend that you read through just the sections you like.

There are also -- as Bill mentioned, there's a significant section of the release that talks about the accredited investor definition and questions about the rules, who -- that limit who can invest in certain offerings. It's pretty binary right now for the most part so, you know, you're either accredited and you can invest or you are not -- a non accredited, and then your opportunities are much more limited. So we asked bigger picture questions about how we should approach that, whether it's appropriate to expand the universe of accredited investors or have some other way to allow currently non accredited investors to invest in more private placements or exempt offerings, and we -- we want to really probe on whether it's appropriate to look at something other than just the wealth of the investor in making that determination, so there are questions drawn -- a lot of it draws from the 2015 staff study on the accredited investor definition.

We've gone through that in great detail in the concept release, and we ask a lot of questions about whether we should revise the financial thresholds, whether we should look for a different measure of sophistication, investment experience, testing, you know, there's a
Committee if there’s a topic that’s of interest to everyone, that there’s kind of a consensus on, we could all as a committee hear from different perspectives and that would be a full committee agenda item. If we thought that there was a discrete topic, for instance, maybe it is how to sell securities over the Internet, which would encompass Crowdfunding, 506(c), Reg A, maybe we look at a subcommittee for something like that.

And the other thing I would just like to mention is that I am, you know, really in favor of looking at the whole exempt offering framework as a whole. The first 30 pages of the concept release really do talk about each of the different exemptions. I have a chart here that I can barely understand as a security lawyer. I think it would be a great opportunity. We’re in a unique situation right now as this committee to just take a step back and look at if we were developing the – the exempt offering framework from scratch what might be our recommendations.

And on that, I am – Jeff had some comments, and then we’ll open it up to the committee to talk about the ways you’d like to approach this.

MARTHA LEGG MILLER: And if I can jump in quickly before Jeff. Since we got off to a little bit of a bumpy start with audio, which it sounds like we’re in good shape now, I did want to add in a lovely standard disclaimer that we give at almost every event you’ve heard anyone from the SEC speak at, which is any statements made by SEC staff or commissioners or any speakers from the agency or their own perspective are not necessarily reflected of the perspective of the entire Commission. So I just wanted to add that lovely disclaimer, and so that we can skip that in future notes from staff for the rest of the day.

CARLA GARRET: Thank you.

JEFFREY SOLOMON: So I would just say my views are just my views, and not the views of all my colleagues at Kain.

So I think there’s – first of all, the framework that Carla has laid out I think is a great one. If we’re going to function, I agree with you, sort of figuring out how we break this down because it is an amazing document. But it took me and my team quite some time to really break down where we wanted to lean in and how we wanted to think about it. And I think there’s a natural place.

Certainly looking at the accredited investor as it relates to investment vehicles is one whole area that when you think about the two sides of capital formation, right, the investor side and the...
CARLA GARRET: Okay. Thank you.
Do other members on the Committee have suggestions and thoughts on the harmonization concept that they'd like to talk?

(Ms. Hanks indicating)

CARLA GARRET: Hi, Sara.

SARA HANKS: Yeah. Hi. I just wanted to raise one point with respect to the breaking off discrete pieces because I think that one of the things I love about the concept release is it looks at everything as a whole and says how does all this work together, and I worry about, I mean, this committee and its predecessors have been very much in favor of expanding the accredited investor definition.

One thing I worry about, though, is if you look just at the accredited investor definition, you've got the possibility of distorting the whole process, and what I mean by that is my guess from practicing in this area is that if you did -- if you took some relatively small tweaks around the definition of accredited investor, especially around the sort of who's sophisticated, you could take the -- you could increase the investor -- accredited investor potential pool by, I don't know, maybe 250,000, 500,000 people. It doesn't seem like a lot when we're talking about 12 percent of the households in the states being -- being accredited, but only about a half a million of anybody who is accredited actually invests in Reg D offerings, and so making a relatively small tweak to the accredited investor definition could increase by 100 percent the people who could invest in Reg Ds, which makes Reg D way much more attractive. It's already a lot more attractive than registered deals, more attractive than Reg CF, more attractive than Reg A, and so what you're doing is you're saying, let's make this the more attractive to the issuers, and then you're leaving behind all of the retail investors. And I know the chairman has been concerned about that. This is one of -- investing and securities is one of the two ways that you make money, that you have wealth. The other being real estate. And so I do worry about there's going to be these whole bunch of people who are going to be left behind -- left behind, which is why I love the idea of pool investment vehicles being a possibility to exit -- to expand that, and make Reg CF/Reg A more attractive, but I do worry about if you spin off, that is a discrete thing. You've just skewed the whole -- you've changed the facts on the ground.

JEFFREY SOLOMON: And so I actually think you're 100 percent right. This has to be integrated, and the great thing about this is it's actually called harmonization release, which is awesome, so we should -- if we're going to split it and take a look at it and do deeper dives, I think we have to come back together as a committee to make sure it all works together 100 percent, otherwise we can end up with some real distortion, and I agree with you, that's not -- that would not be the goal. We kind of defeat the whole idea of harmonization, but I just think if we're -- for -- for me, for example, I am -- I -- I don't do this every day.

We have people in our organization who could really go deep in both sides of this.

and I'll be drawing on a lot of their expertise in order to make sure that we're -- you know, as we think through all the unintended consequences. And I just think to me it's just -- it seemed like there's a natural break point, but I agree with you. I mean, between sort of cap -- dealing with investor issues, and then dealing with issuer issues, but if -- but we have to bring that back together again, or we could end up with a very skewed and un -- again, unintended consequences like the one you highlight, which would kind of be -- it would be -- it would defeat, I think the whole purpose of -- of being balances, so I totally agree.

CARLA GARRET: I also agree with you. I think that the pulled investment, I think looking at the crowdfunding Reg A, 506(c), looking at the vehicles where non accredited investors, even with an expanded definition of accredited investors are able to invest is incredibly important, and something that this committee can provide valuable input on.

JASON SEATS: One quick reaction. I am wondering almost if maybe there's three things to think about. The first is the definition of the -- who those pools of investors are, and then the other two are related to activities around them. One is the activity of...
going and raising pooled capital, and the other is the activity of going and raising new issuer capital, and so and so and so and the suggestion to start with the definition of accreditation makes sense to me that maybe there's actually three things there, and putting the work into the definition of the investor pools, who these people are, like maybe -- maybe that is a thing by itself, and then you have two activities.

Because one is defining people, and the other is defining behaviors, right?

CARLA GARRET: Yes, I agree. I do. Because we do have to define the two -- there are at least two different buckets of investors, and there may be more that -- that you define, and then you define whether or not they are -- which way they are investing.

JASON SEATS: Yeah.

JEFFREY SOLOMON: So one of the things that we talked -- that we've talked about is actually along your line of -- of three. You know, any time we talk about capital formation, at least in my firm, we talk about three different constituents. And actually, when I presented it to the -- to the investor Advisory Committee, or the investment management, the investor Advisory Committee a few years ago, I always look at some principles that maybe we should focus on first, how to improve them. Part of me wonders are there those -- you know, all these terms, and, you know, it seems like we're talking about existing frameworks and rules and the 40 Act never really contemplated this idea of being able to have a mass affluent or high net worth individuals access private investments or capital.

investors, companies and intermediaries. And obviously we do a lot of intermediary work, and -- and so I -- there is -- there are ways to create good incentives, and not so good incentives for intermediaries to act certain way. I think one of the things we look at here as you -- as you enable different pockets of capital to get access. Almost invariably they are going to come through an intermediary.

And they -- they -- unless they go direct to Crowdfunding, which they could do, but even there, the Crowdfunding site is effectively acting as an intermediary. And the truth of the matter is, intermediaries can -- if they do their jobs, they screen for high quality. They should be screening for high quality, and -- and so that actually creates -- when you think about most of the way the capital gets formed, the very majority of even professional investors, they look for an anchor, right, and then they'll come in around an anchor who they think might be smarter than them in a particular area. And so I think one of the reasons why a lot of investors get crowded out is because they don't actually get access to the high quality deal flow. They just -- they don't -- they never see it, and it all gets -- it all gets angled towards accredited or super accredited frankly at best. And so if we're going to think about this from an investor standpoint, I think creating pooled vehicles that intermediaries can then articulate to their -- to their constituents is actually a great way to bring it back to the appropriate function for screening. And -- and we've talked a lot about this. Reg G and private placements are not the favorite ways to go to retail investors because you've got K-1s and a bunch of tech stuff, and so almost invariably intermediaries don't like to deal with them, and it -- and it knocks out most of the retail distribution in -- in the country because private placements mean K-1s, and K-1s mean delayed tax filings, and you end up in a bad spot.

So if you look at where a bulk of the money has actually been raised, and we just talked about this actually earlier, it's been through interval funds and registered investment companies, and there's a bunch of rules in there that actually preclude earlier stage investing.

And actually because they never -- the rules and the 40 Act never really contemplated this idea of being able to have a mass affluent or high net worth individuals access private investments or capital.

It was much more towards publicly traded vehicles and mutual funds. But if we could figure out a way to again look at -- at some of the existing 40 Act areas and make those easier for intermediaries to essentially screen and sell to high net worth, all of a sudden you really democratize that capital raising function again, and we almost have to think about Reg D. Getting away from Reg D in some capacity and private partnerships because it -- I just will tell you, most intermediaries won't even -- won't even touch it at the mass affluent level. Not even high net-worth level, but not even the mass affluent level, or the -- or the retail level, so it's just something to consider.

CARLA GARRET: Thank you, Jeff. Robert?

ROBERT FOX: Yeah, I've been sitting here listening to this conversation, and I've been trying to think about -- you know, I -- I keep hearing as a non attorney, you know, we -- we talk about Reg D and those -- you know, all these terms, and, you know, it seems like we're talking about existing frameworks and how to improve them. Part of me wonders are there some principles that maybe we should focus on first,
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right? You know, first start with a blank sheet of paper. Are there principles we should focus on first that would be kind of -- maybe set the framework for rule making. And when I think about a lot of these standards, it seems to me that a lot of them were created from an investor protection mindset, right? Something probably happened that they took advantage of somebody, you know, either an intermediary was, you know, not acting at the best interest or, you know, somebody got swindled or somebody lost money or something like that, and it seems like that's where a lot of these issues have come from, at least from my perspective. And I am wondering if it wouldn't be better for the Commission -- or for the Committee to maybe think about some of the principles of investor protection, right, that would go -- that would kind of filter through the definition of accredited investor, or some of the other rule making. You know, if we can think about some of the things that would balance -- you know, what are the principles that would kind of govern that and could balance the need for appropriate capital raising and investor protection. If we could come up with that, it seems like that would provide a framework that a lot of things could be built off of, and I -- and I think that that echoes both the

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intermediary point that Jeffrey was talking about and, you know, the definition part that you're talking about, but it just seems to me that that may be something if others agree, that the Committee can maybe think about because I feel like without that we're just kind of talking, you know. Well, how do we improve Reg D or how do we improve Crowdfunding, or whatever it is, and I'm not sure that that -- that may be an incremental improvement, but I'm not sure that that's a wholesale improvement.

CARLA GARRETT: Yes. Youngro?

YOUNGRO LEE: Yeah. I'd like to suggest, if possible, us -- this committee taking as practical position as possible, knowing the realities of rule making, and not just with the SEC's level, the legislative level. And the reason I say there's twofold. One is we talked about harmonization, and like Jeff talked about, it's very, very difficult for mainstream investors and companies to invest in companies that access that and intermediaries don't even try because it's so hard. So the elephant in the room, in my mind, is kind of the whole point of the harmonization, which is there -- there is regulation Crowdfunding. There has been three plus years of operation. There has been a track record. That's

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what the SEC spent so much time writing on. And as you guys saw, the AIOYP release that our -- the Committee of Online Investment Platforms have -- have -- have submitted and said throughout this committee. That's, like so -- so we're not -- I guess from a -- I am overly simplifying, but instead of trying to come up with maybe a brand new suggestion on harmonization -- and maybe this is what Sara was referring to. We have a track record, just like a credit investor definition is a very specific thing that the SEC is looking at, which I agree with to make changes. There are very specific limited changes you can make to reg -- Regulation Crowdfunding today immediately that will -- that will very much expand the data points, the usage and everything else that I think will be more helpful, so that would be my first personal, and in a -- from my perspective obviously as the -- one of the very few portals that are operating this kind of industry, just focus on what's actually possible and what -- what's there today.

And then the second bigger point of this is I know that previous committee has spent a lot of time and effort in all of this. My understanding was essentially none of it was acted upon, or -- or was addressed by the SEC. So it's a very direct point,

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maybe a question to the SEC because I would like to understand what is constant. Right? Like if the -- if the answer really is. That's great, all these things is great, but really a credit investor is that and needs to be worked on, that's fine. I can -- I can personally kind of even set aside the Reg CF changes, which -- which I think are very easy, relatively speaking, and just focus all in on the credit investor so that we can give the most helpful advice and feedback on that specific point rather than us trying to come up with, again, a lot of different things that after another year of doing this, frankly nothing is going to happen.

CARLA GARRETT: Thank you, Youngro. I actually agree with both -- both of you, Burt and Youngro, which are we could actually do both if we wanted to as a committee. There could be a focus on the various practical specific changes to certain of the rules, like Crowdfunding or Reg A or other 506(c). There could also be that the committee does look at the big picture, and at the principles of -- of investor protection, and we couldn't -- can do both if that's something that the committee is willing to do, and something that they are interested in doing.

That would be something I would be interested in
that's great. You know, do I have a sense of timing?
I don't. I don't control the agenda, but that being
said, it will filter through us, and we will try to get
that out as soon as possible.

To Burt's point about investor protection, that's
something we take on every single day. That's how we
function. That's part of our core mission/mandate.
Whatever you guys provide, I assume it will be within
the constructs of your -- your mission, your -- your
statutory mission, your bylaws, your charters, but also
through the lens of, you know, what would be helpful
for us to kind of fill our job. And don't worry,
well -- well take a look when we also make a
termination through the lens of how does it facilitate
cap formation, protect investors and maintain fair,
orderly and efficient markets.

So I think this is already very helpful because
you guys have identified kind of the key players and
the key themes. If you guys do take this one, I think
you'll provide a really valuable input for us in terms
of what steps we can later take and what the division
will do, so, um, I have really been heartened by this
kind of conversation, and -- and look forward to
anything that you will do.

CARLA GARRET: Thank you.

ELAD L. ROISMAN: Sir, and, look -- first of all,
again, I'll echo this later, but thank you all for --
for coming here. And, look, this discussion already
is very helpful because it goes to show the different
perspectives you all provide and -- and bring given
your diverse backgrounds. I think everything here
said, even though it may seem -- have been a little
bit in a different direction. I think they're all
valuable. Look, we're going to take your input
because you guys have unique perspective and
background, and the reason you were formed as congress
determined that you guys were an important input, this
committee has important input in terms of our agenda
and what we're trying to do. To the points about like
how can we improve the private markets, but at the
same time be cognizant that if we improve the private
markets, it may have an impact on the public markets
is something that we're constantly thinking about. I
don't think that we should stop that because I think
we need to work on both on tandem, and I think
anything we do in one will have an impact on another,
but we should think about that as we kind of draw out
our agenda.
To Youngro's point, like, you know, I personally
would love any input you have. Even if it's simple,
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<td>1. there a natural progression from some of the smaller exemptions where you're raising less capital to the larger ones, or is there something there that we're missing? You know, are the amounts that are -- are currently available for the different levels of offerings the right amounts for smaller companies? I think all those things -- you know, as an organizational theme for the work that we get from you would be really useful, to have that idea that this is what small businesses are looking for as they're using our exemptions, and in what has been highlighted in the release.</td>
<td>1. smaller businesses somewhat is the idea that should we be relating offers? You know it's one big idea that reaches across all of -- main -- basically all of our exempt offerings today. Do we need to regulate offers, or do we want to just regulate the sale making sure that folks have sold to the -- the right group. Because if you do that, then it makes it so much easier to reach out and to use the Internet, to use social media, use different ways that people use today to find people, you know, more broadly, but then you just limit the -- the regulation of to who you're selling to. He ultimately has protections around that.</td>
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<td>JEFFREY SOLOMON: So I would be curious to know, you know, when a small business goes to raise money. I mean the ones that come to us are probably a little bit bigger and have already done a few offerings, so I -- I will just say I don't have a lot of understanding of when a small business says, I want to go raise money. Have they even thought about how they would go about doing that from a regulatory standpoint? My guess is probably not, so they ask their attorney, and their attorney gives them the advice on the best exemption to utilize. And can we just level set, is that generally how it happens?</td>
<td>That's a big -- one of the big ideas that's in one release. It's one that, you know, your perspective thinking about that from a smaller business's perspective and the friction of trying to avoid a general solicitation of an offering. That would be pretty useful for us to hear from you on.</td>
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<td>HANK TORBERT: Yes.</td>
<td>CARLA GARRET: Uh-huh.</td>
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<td>JENNIFER ZEPRALKA: Yes.</td>
<td>HANK TORBERT: Could we form a special subcommittee on this specifically, if you will, to -- to review this, the framework for this particular part?</td>
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<td>HANK TORBERT: Yes, it's -- as the president of a small business, I will tell you the answer is very simple. This is a very complex -- very complex situation. As a small business, we would not necessarily consider some of these things because one of the costs -- the amount of investors we actually have access to, the disclosure requirements, it may be too much versus a very simple debt equity raise, which is -- and also, as you look at the accredited investors and who we have access to, I think it's too small. If we can just make minor tweaks to the existing system just to allow for us to reach just a smaller group of people. For all small -- smaller businesses, that could be a significant change if I'm making any sense. Just a small tweak could mean millions, perhaps hundreds of millions of extra dollars that are available to a small business, and so if we could look at that -- but in terms of how we view the world, a lot of these are just too expensive for us from an accounting standpoint, from a legal standpoint, it's just too much.</td>
<td>CARLA GARRET: Definitely. I mean, that's what we're here for is to -- to set up what is this committee interested in. We're all going to be interested in different things.</td>
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<td>WILLIAM HINMAN: One other big idea that's useful here that's being asked for a comment on in the release that would, I think, simplify things for</td>
<td>HANK TORBERT: Right.</td>
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<td>CARLA GARRET: -- we can definitely put together a subcommittee on that.</td>
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<td>HANK TORBERT: Okay.</td>
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<td>HANK TORBERT: Yeah.</td>
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<td>CARLA GARRET: Okay.</td>
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<td>HANK TORBERT: I said, Is it possible? I mean, we were earlier discussing if we should break into smaller groups, if you will, whether it's investor protection or whatever the case may be. But if there's a way to -- especially from a small business standpoint if there's a way to form a small committee that would look at some aspects of this, if you will, that he's discussing.</td>
<td>CARLA GARRET: I mean, that's what we're here for is to -- to set up what is this committee interested in. We're all going to be interested in different things.</td>
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<td>HANK TORBERT: I mean, some people are going to be looking at one way, some people are going to be looking at other ways to raise capital for small businesses, and we can -- for people that are interested in focusing on one, you know, kind of unique topic --</td>
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<td>HANK TORBERT: Okay.</td>
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<td>CARLA GARRET:</td>
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<td>HANK TORBERT: Okay.</td>
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JEFFREY SOLOMON: I actually have a question. I actually — I read that in the release, and it seemed like a really big idea, and then I will just say it's something I've ever contemplated looking at the offer versus the sale. I did — I never really — I never really thought about it because I always viewed them all — when there's an offer, there's a sale. And, I mean, I kind of view it as one together. And so I just would be curious to get a little bit more color on some of the things that you're thinking about and where we can potentially get pushback. I hadn't really thought about it, but it seems like an interesting idea, I just — I am not sure how that works.

WILLIAM HINMAN: It's certainly the 506(c) exemption, right, where you can do a general solicitation offering to anyone, but only sell it to accredited investors. It's sort of that concept taking that more broadly than just one particular rule. 506(c) raises some interesting issues around verification of have you told to the right people at the end of the day. But that's — that's the general thought is we are less concerned — we would be less concerned with who you — who might see the offer as so how do you draw the lines between them, but that's one of the things we're asking for. I mean, again, we need it here at the outset. Is this something that actually attractive to smaller businesses, is the idea of having to limit themselves in how they communicate and making sure they're not engaged in a general solicitation at the front end something that's really burdensome and is creating real problems or maybe it's not? Maybe they know how to do a private placement without, you know, how to find their investors.

So we're just asking the general question, is the regulation of the offer, as opposed to the sale something that's problematic, something that could be revised, to the extent we do think that, then there would be some integration things to —

JEFFREY SOLOMON: Also, I would just say we're giving advice all the time on how not to do — how not to integrate and our clients are like, What are you talking about? Like — so I don't even think — again, small businesses aren't necessarily thinking about integration rules. It's usually when you get an intermediary or a lawyer involved they are like, Whoa, whoa, whoa, whoa, you can't do that.

WILLIAM HINMAN: Uh-huh.

JEFFREY SOLOMON: And here's why, and they're like, Really? I've been talking to — I've been talking to everybody, right, and then you — and then you scramble to figure out, okay, Well, who did you talk to, and — and are they all accredited. It becomes a real thicket, a hornet's nest, if you will. And so, again, one of these — it's just something that we have to deal with on the intermediary side when we first engage with somebody and try to figure out, okay, how many people have you talked to about this. It's a — it's a big issue that we have to, I think, resolve. So that's — that's — that's helpful.

CARLA GARRET: Okay. ROBERT FOX: So I think that Bill's point on the offer is — is probably a more articulate way of what I was trying to articulate in terms of some of the principles, that it feels to me that if this committee could focus as well on things like, hey, maybe if — if, you know, we can still get yet, you know, things done in an appropriate regulatory context without regulated offers, are — you know, maybe up to a certain amount, we don't have to have an accredited investor. Whatever it is, I think that there's some things like that at a higher level that if we can establish that we think that would be very beneficial.
to small businesses. And also to make sure we're
clear, I think the definition of small businesses
up -- is -- is a pretty big business, right? It's not
your mom and pop dry cleaner, right? And, you know, I
think -- I think that would be very helpful. I'm not
trying to discount that I think that there's some
knowledge that this committee can provide some very
concrete, discreet changes that would also be
impactful, but I feel like if we can say, Hey,
overall, small businesses that would really benefit
from, you know, some overarching print, you know,
things here that we think if the SEC kept that in mind
as they're writing the releases and got an anchor back
to that, it would be very helpful.

CARLA GARRET: Thank you. Yes, Catherine.

SAPNA MEHTA: Just one more point on that. I
think it would -- might shed some light on
how we treat some of this.

CARLA GARRET: Thank you. Yes. Sapna.

SAPNA MEHTA: Just one more point on that. I
know we were looking at it from the small business
perspective, and not from the investor protection
standpoint. That's not our role, that's your role, and
you will thoroughly look at that. But just -- you
know, I think going back to Robert's point it would be
helpful to get a refresher on the reason for the
framework for having general solicitation rules
because if we're loosening general solicitation rules
the offer side of it, and loosening the -- or maybe
not loosening, but making more appropriate the
accredited investor definition, you know, we might be
taking -- the pendulum would be definitely swinging in
the other direction. And also just from a company

JASON SEATS: I have a -- a comment. I like the
idea of separating out the regulation of offerings
from the sale and opening it up thinking about Jeff's
comments about the dynamics of fundraising, which is
what we experienced a lot. We have a portfolio of
thousands, and they're -- we engage with them when
they are, you know, three founders and a -- a dog in a
garage. I mean, the way that they -- the way they
just -- they raise money is they ask a friend, they
ask an adviser and they get good advice, they get bad
advice, and we hope that they find someone who gives
them good advice, but I think that they -- the
indirect benefit, not the direct benefit, I think the
indirect benefit comes through the intermediaries.
And I think that by opening up the offering what
you're actually doing is creating a lot of flexibility
for the way that intermediaries help those companies
raise money. And so it -- but by itself it doesn't
solve the problems, but I think it removes -- it
removes one important friction point, but because
it's -- you can tell that we haven't thought about it
deeply, it may have some unintended consequences
and/or dynamics that it will create that we don't
think about.

One of which is the fact that the best companies,
the ones that are in strong positions to raise capital
don't market the fact that they're raising capital.
And so you'll have a bit of adverse selection, which
is why I think opening up the restrictions on offerings
coupled with increasing the flexibility of accredited
investors to put money into pooled vehicles that are
intermediaries who may have the access, that a
dual-pronged approach sort of makes a whole lot more
sense to me than opening it up and assuming that
companies are marketing themselves directly

CARLA GARRET: Thank you. Okay. So I think we
probably should maybe end the harmonization talk right
now. It's -- in terms of November meeting, I think
we have a lot of different ideas on how to structure,
and what the different points are. I -- and if there
are special subcommittees that we think would be
useful, maybe we can talk about that offline, Martha,
unless you think we should determine that today.

MARTHA LEGG MILLER: We can come back with the
general session this afternoon if everybody wants to
just -- now that we've had a chance to float ideas. I
know most people like to take a minute --

CARLA GARRET: Okay.

MARTHA LEGG MILLER: -- as opposed to jumping
right to formulation of an idea --

CARLA GARRET: Okay.

MARTHA LEGG MILLER: -- but we could use some of
that if folks have specific leanings on that.

CARLA GARRET: Okay. Great. Thank you. And
today thank you again, Bill and Jennifer. That's -- there's
a -- there's a lot of um -- um, very interesting ideas
for us to think about.

Our next agenda item is SEC's proposal to amend
financial disclosure requirements relating to

acquisitions and dispositions of businesses.

On May 3rd, 2019, the Commission released a
proposal to amend the financial reporting requirements
for the acquisitions and dispositions of businesses
including Rule 305, 314 and Article 11 of
Regulation S-X. The proposed amendments are intended to
improve for investors the financial information about
acquired and disposed businesses, facilitate more
timely access to capital and reduce the complexity and
cost to prepare the disclosure.

In addition to hearing from Director Hinman on
the technical elements of this rule, we're also going
to be hearing from some guest speakers.

Also, I just want to note that one of the
purposes of what we hope to accomplish during -- before
our lunch time is to not only hear from the speakers and
hear from Director Hinman and to ask questions, but
we're hoping to set aside at the end maybe 15 or 20
minutes to actually make, if we can, and vote on
recommendations with respect to these rules and what
our committee would like to recommend to the Commission
with respect to the rules.

So think about that as we're listening to the
speakers that we will be hopefully voting on a
recommendation before lunch.

I'd like to introduce our two speakers. Thank
you for coming today. We have with us on the left,
Matthew Swartz, who is a partner at Pillsbury,
Winthrop, Shaw & Pittman. Mr. Swartz has over 20 years
of experience in providing legal advice to middle
market and technology companies and their investors on
mergers and acquisitions, venture capital and private
equity transactions and public securities offerings.

Chambers and partners notes that clients praise
Matt's encyclopedia knowledge of business law. Matt is
a published author of securities law and SEC
compliance. He is a graduate of UC Berkeley and UC
Hastings College of Law. Welcome, Matt.

MATT SWARTZ: Thank you.

CARLA GARRET: We also have with us today Bill
Korn. --

BILL KORN: Hi.

CARLA GARRET: -- who is the chief financial
officer of MTVC. Mr. Korn is a veteran technology
executive with over 30 years of experience managing
high tech businesses. MTVC is a provider of
electronic health record software and other IT
healthcare solutions.

Bill graduated from Harvard College with a BA in
economics and received his MBA from Harvard Business

School. He has served as CFO of seven companies, has
raised over 350 million of capital and has completed
multiple acquisitions. Welcome, Bill.

BILL KORN: Thank you.

CARLA GARRET: First we're going to have
Director Hinman provide an overview of the rule
changes, and then we're going to have Matt and Bill
speak.

If I could ask Matt and Bill because we are
running a little bit behind, if you're able to limit
your -- your time to about ten minutes, that would be
useful. So, Bill.

WILLIAM HINMAN: Right. Thanks, Carla. And I'll
limit my time just because you have two very capable
speakers here, but I did want to get a little bit of
an overview of the rules particularly significant for
smaller businesses either on their way to becoming
public companies or when they are public companies.

Even small business that never become a public
company, but sell themselves to the public company are
affected by these rules. These are the rules that the
acquirer will have to comply with after they acquire
that small business, and today they're very complex.
The interpretations of these rules that exist today in
terms of what you have to provide in terms of
background on financial statements of the companies you are acquiring are -- are not only complex, but they take up about half of our financial reporting manual in terms of the interpretations that have been issued under those rules. 

So what we're trying to do with the Rule 305 and some of the related changes is to streamline that, to simplify that and to just make, you know, more sense of these highly technical rules, which you'll -- you'll hear more about. One of the things that these rules trigger off of is whether your acquisition is significant or not, and at what level is it significant, and there's been three tests that have been used historically for that, and you'll -- you'll hear more about these. There's been an income test, an assets test and an investment test.

The investment test was not designed to say how -- how big a deal is this, what you are paying versus historically it's been your -- the amount of assets you have. We have thought about that and said, You know, how much you're paying versus your assets it's maybe a little bit out of step without -- as a measure of significance generally, that your assets may not relate to the size of your business or how significant this particular operation is, so we're revising or suggesting to revise that to look at how much you're paying versus your total worldwide market cap. I think that's a simple change to make, it's an easier number to calculate, and I think it -- it makes more sense.

The other significance test that we're looking at changing is the income test, and that we looked at the relative income of both the acquirer and the target. And there if the acquirer happened to have a near break-even year and you looked at that as a denominator and you put the targets asset -- or income on top, that could be a very significant acquisition if you've had a near break-even year or if you had a loss -- a small last year. And so we get a lot of anomalous results, and so we're changing the income test or suggesting that we could change the income test to add a revenue layer. And so you look at both revenue and income in that component when the -- the income is not a good measure itself, and that should result in fewer anomalous situations where historical financials are required.

Another thing we're doing is how many years of historical financials do you need to prepare. Depending on significance, that might be one, two or three years. With the new suggestions we're going to limit no matter what the level of significance -- significance might be to a two years of historical financials. That will make it easier in many cases to prepare. We think investors are really more interested in the last couple of years, and when you go back three years, the relevance there seems to be much more limited and people are making investment decisions based on performance over the last couple of years, so we're looking at that. We're making some changes that should be particularly helpful in the IPO space, IPO companies now have never sort of integrated some of the financial statements of the targets that they've been rolling up as they get ready to go public into a public filing, and because it hasn't been previously publicly filed, we require a lot of these 305 financials for these roll-up situations.

We're going to say going forward if you've integrated that company for over a year, you won't have to supply the proformas and the historical financials of the target stand alone that IPO companies used to have to do. That should make it much easier to -- to join the public companies here. There's some also -- there's some changes that relate to the proformas that also accompany these presentations. If you have a 305 historical financial obligation, you also have an obligation under Article 11 of SX to provide a proforma financial status. It's basically the last full year for the two companies combined. And it hasn't been given a lot of attention by investors because it's -- it's somewhat of an -- an artificial set of numbers. It's, you know, the last year, putting the two companies combined, what would you do in terms of the accounting changes that happen and here's the result. It can be useful for analysts and -- and people certainly will look at it, but it doesn't really give you an idea of how the combined businesses will operate going forward. It doesn't cover the potential synergies of the -- of the two operations, and so we've asked for comment on whether it would be useful to have a separate column of the pro forma financials that look at management's expected synergies, or changes as a result of putting the companies together.

That's generated a lot of comment. Those synergies typically have been discussed when people talk about their acquisition strategy outside of the registered filing. The registered filing has the very dry proforma, and the rest of the story gets told outside the filing. So we've suggested some rules that would require more of that story to be told in the filing. Some people are a little bit reluctant to put
I've been honored for inclusion by chambers and partners in the top M&A lawyers in the Washington region. My favorite observation from Chambers about me sits on my refrigerator for all of the household to see, and I quote. Always thinks things through from a reasonable market perspective of what's fair. So I hope I can bring some of that here today.

I'm going to try to honor the request to stay within ten minutes, and the first thing I'll do is say if I had to -- well, let me speak to my experience briefly and say I'm counselor mostly to small and middle market companies. Many of them are technology companies, not all of them are. I have counseled on probably 150 exits by small and middle market companies, and I will be speaking primarily from the perspective of a seller who is evaluating options as a small business person to exit to the available buyers in the market, and how these rule changes look from the seller's point of view. Having served as a corporate director of two middle-market companies that exited and sold to public companies I feel that I've seen this process enough that I hope my perspective will be valuable.

So if I could summarize the proposed rule changes in one word, it would be Bravo. I think the small

business community, both the small business issuers and also the targets are very much in favor of the reforms that the SEC has proposed in this proposed rule change. If I had to summarize it in two words, it would be Bravo however, and I'll proceed with the -- with the however now.

Let me begin by giving you a little bit of context in the process that middle market and small companies experience when they're looking to sell. And, again, I'm speaking from the perspective of a selling company and the impact of these rules on selling companies. Small business people have limited options for exits. Initial public offerings, as I know the Commission is aware from some of its other work, have become more and more expensive. Private equity has become more and more active, different aspects of the public offering process are in different ways more expensive, more cumbersome, less available to small companies. So the M&A exit is more common than it ever was, and it was always pretty common. So I'm going to speak to what we might call a managed process, or a process led by an investment bank, not because that's the only process, but because it's one that quickly kind of illustrates what the issues small companies face even without an investment bank actually are. In a managed process an
the transaction altogether. So an audit is a risk. An audit is a diminution in certainty. So who are the kinds of buyers that are available to small and middle market companies. Private companies, investment funds, and I'll include private equity in that, and public companies, but as we all know, there's more than one kind of public company. They are small public companies and big public companies, and I think if there's a message that I'd like to convey from all of this, the small public companies are put at a substantial disadvantage as buyers of small business targets, and the reason for that is that the significance test I submit even as changed, though certainly is unchanged, impose a requirement that larger public companies won't have simply because they have such great assets, income, market cap. It takes an enormous target for those significance tests to be met.

So the rule certainly affects public companies as buyers, but I think it's useful to focus on small public companies because they're the ones who really are impacted by the significance test simply by virtue of their size, their smallness. So I have here a table that -- sorry, among the issues that are on the table when small company entrepreneurs or boards are evaluating alternative acquirers, can you see the resources? I mentioned this. Yes or no. Yes with public companies. Is there a delay that's likely to threaten the certainty of closing? With large public companies, the answer is almost certainly no, and I'll use examples just randomly chosen, the alphabets and Johnson & Johnson's and Marriott's would take a tremendously sized target for significance tests to be met. So the kinds of requirements that the rule has proposed or has modified would impose do not apply to companies like that because it's so hard to reach the significance tests. On the other hand, smaller public companies, you'd have to be even a lot smaller than that, really to have that issue. So they're less competitive at the table when selling companies are evaluating competing offers, and I submit less likely to buy the company, and therefore because the selling company if it has options that don't involve the uncertainty of delivering audited financial statements are less likely to choose a small public company as a buyer. And I think it's a matter of securities law, but also of -- of common sense. One choice or two choices, a private company acquire, a large public company acquire don't have this burden and delay.

Small public company acquire has this burden and delay.

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So even if the prices are the same, a seller is likely to choose anyone but a small public company as the acquirer. So smaller public companies are just less competitive as buyers.

So I'll skip right to will the proposed rule changes make it better? Yes, but diminishing the likelihood of a significance determination with the revised rest and the burden on target companies that changes what has to be delivered. At a separate topic is the IPO process, but I think the proposed change to the rule that deals with allowing IPO companies to under certain circumstances pre -- admit pre acquisition target financial statements is probably more of a benefit to the IPO process than it is -- that it is to the M&A process, but that's another story. I still think that's a particularly good change and helpful to small companies going public.

Will the proposed changes make small public companies more competitive as acquirers? Yes, probably, but they are still at a disadvantage relative to other common buyers.

So I'll go on and say, This is a good step, but what else could the Commission do. Move farther away from the audit requirement of significant targets, meaning significant with respect to the buyer, place more emphasis on detailed proforma information and explanation. So Director Hinman's comments about projected proforma synergies is -- is exactly what I think could be the most helpful, though I'm sure in -- in the comments that the Commission has already received the disadvantages are real and this is what accountants call the tension between relevance and reliability. I think if you were to look at private equity buyers and asked, What are you looking at when you're looking at buying a company, I would bet that the first thing they don't say is audited financial statements. I bet one of the first things they say, and one of the first things I've observed is what do these companies look like once we buy them. Are we paying a better -- are we buying low with the hope of ultimately selling high? And so that's a proforma analysis, and the negatives of that, of course, are that the cost savings are not necessarily things that acquirers want to make public either because they're distasteful or because they are competitively sensitive. Nonetheless, that is where the investment decision is made, so I go on and say, Well, it's -- I had a bullet point in this last slide when I first drafted it saying that private equity is a competitor of capital markets. That may be a little bit more than
is the case, but it's certainly true that the rise of public equi -- private equity has come just as the fall of IPOs has -- has been seen. So I think it would be useful for the Commission, and you may already be doing this, to study the financial diligence of the competitors. Who is the competition? It's private equity funds. What do they care about? And they care about relevant information. Reliable information in the audits are good, check the box, highly reliable, always part of the Commission's important role of protecting investors, but is it relevant enough that sophisticated people make an investment decision on that alone? I submit that it is.

I am happy to discuss more. I want to respect the time limit. I want to thank you all for having me as your guest. Thanks for your service to the country the time limit. I want to thank you all for having me as your guest. Thanks for your service to the country

CARLA GARRETT: Thank you very much, Matt. Bill?

BILL KORN: Thank you, and I've also got some -- some slides. I'll give you all a very, very brief introduction. MTVC does fit that -- that profile of a

small company. When I joined the firm we were a $10 million company. A year later we went public. At the time that we went public we were still a little over 10 million. We bought three companies in the day of the IPO. Last year we did 50 million in revenue. This year where we're at we're projecting 63 to 65 million. And we've done 15 acquisitions over the -- the last six years, and eight of them have required us to -- to file the -- the 305 or the -- the small business version, the 9 804 financials, which are virtually the -- the same.

And so I'm going to give you some advice, you know, from -- from my perspective. I agree that these changes that are being proposed will be very, very welcome. You know, I think there's a few things that we might be able to tweak that would make it a little more useful for us. I don't know if these slides can -- can come on, but from -- from my perspective --

Okay. There we go. Background.

From my perspective, the -- the one of the challenges we face -- again, it's been -- been mentioned. When I talk to analysts, when I talk to investors they never ask me about the 305 financials, and they almost never ask me about the proformas. What they really want to know is how's that going to change you, what will that do to your revenue, and more important what's it going to do to your profit and your cash flow in future years. And so I think what we want to -- we definitely want to respect getting those financials out there. We need to think about it and not spend more energy on certain aspects, and, you know, again, I'll -- I'll talk about acquisitions. You can either buy the stock of a company or you could buy the assets. We've done exclusively asset purchases.

So I'll file financials, I'll show the balance sheet of the company that I bought, but I didn't buy the balance sheet. I didn't get the cash, I didn't assume the debt. And by the way, even in my proformas after one quarter it's part of my business, so for the next two years I've done all this work to want to come up with a balance sheet, and we're not really using it. And, you know, the other thing -- that hurts us the most, I think -- and again, maybe five suggestions, this is the first of them, is that when we file the -- the financials, the good news is 74 days we've got it filed, everything is perfect. And then there's a period of time for which we need to keep refiling it every time there's a registration statement. And, you know, to me it isn't so much about is that timeframe in years or three years? Is it nine months? If we could

represent it because you're talking about the financials before we bought the company. And I -- you know, I've had situations where an auditor keeps calling back the -- the same buyer, and he said, I left I left a year ago. You know, I've signed a non compete, I've signed a non solicitation. I agreed I was never going to talk to the employees, I was not going to talk to the customers. Why are you asking me what changed? And so, you know, to me that -- if we could find a way to incorporate those financials without the requirement of -- of getting that representation again, that would be really useful.

So the -- the second recommendation I've got is -- is one of carve out or partial financials. And, again, when you buy assets as opposed to the whole company, you know, the challenge is you spend all this time on the balance sheet, you work on a cash flow, none of
that is actually relevant because you didn't actually buy all of that. And, again, to me that -- the challenge, especially when you buy a company that's years old, you're trying to get a balance sheet. Getting that opening balance sheet when it's never been done before is a big, big deal, and it's not really relevant.

A company that's done acquisitions, you do all this work to figure out how to value those acquisitions and how much is goodwill and how much is intangible. It doesn't actually matter because once it comes into our books, that all gets eliminated.

So, you know, there is currently a carve-out provision, and I've actually used the carve out financial statement rule a couple times. You know, to me I think when you're doing assets, it would be good to encourage carve-outs, and even -- you know, this probably sounds like heresy, but maybe it isn't a full financial statement with a balance sheet P&L in it and a cash flow because, again, you buy a division of a -- of a business. In some ways the cash flow is artificial because they got money from the parent -- the profits they made, went back to the parent and you spend all this time trying to figure that out, and it's not really relevant.

So, again, if you can figure out a way to do partial financials. And, again, even if they couldn't be ordered, even if they can be reviewed, if they were actually relevant, to me that would actually be more useful for the -- for the investors.

You know, on the -- on the income test I think we've had a challenge that others have talked about. You go through a period where you're showing a little bit of GAP profit, you buy a company, you're now amortizing intangibles, you're now showing a GAP loss. So at the end of the year, GAP debt income is pretty close to zero. No matter what I do as a significance test, anything divided by zero is infinity, everything is relevant.

So I think the revenue test, you know, to me, if I was thinking about the distinction between the 804 small business rule and the 305, I would almost say in a small business, make it all revenue. Because in some respects the revenue is going to be more relevant as to how significant it's really going to be in terms of the -- the business. And, you know, if you were going to do a -- a test for a bigger business under 305, again, it seems to me the -- the income before extraordinary items is what's important. And when I think about the financials of the -- of the -- of the company being acquired, if there was impairment of goodwill, who cares? If there was amortization of intangibles, again, though -- that's another noncash expense. It doesn't carry forward, it doesn't even hit the GAP books. I would take those two out. And, again, sometimes we face the situation where I actually have to complete the audit, figure out whether the goodwill was impaired last year or the year before, then I'll know what the net income is. And by that point, now I've got to go file the financials.

It's my -- my fourth suggestion is -- is actually a -- you know, a relatively small one, and -- you know, in terms of the investment test, again, I think using market value makes a lot of sense. You know, I've heard others like I & Line, KPMG suggest using this as the -- the common, so there it would be easy to figure at least if it was converted, what would it turn into preferred that's convertible. And, again, you could at least say if it was converted, what would it turn into so you wouldn't completely eliminate that, and that would be my suggestion for -- for coming up with the -- the investment value.

And my -- my last suggestion really revolves around the performance. And I think the idea of including management adjustments is a good one. Because, again, today when you're the reader of those financials and you see them, I mean, occasionally I'll have somebody say, You know, Bill, is that what MTV is going to look like when you complete this acquisition?

Well, no, it shows revenue from customers who left before we bought the company so we're not going to get that revenue. And it shows a lot of expenses that we wouldn't have so you're not going to see those expenses, so if you could -- if you could put in adjustments -- and, again, I realize it will be easier.
for a company that's already done repeated acquisitions
to be able to convince somebody, okay, I've done this
enough times, you know, I know this is going to go down
10 percent, I know that. But I still think the -- the
only challenge with the adjustments is going to be
figuring out how do you do a comfort letter. Because
at the end of the day we can -- we can convince
ourselves of it. But if my investment banker asks my
auditor to -- to provide comfort, you know, it's like
providing comfort on the weather forecast. You can't
do it, so, again, I think it needs to be clear this is
management's responsibility, but I feel like if you --
if you wind up with it potentially needing to be
comforted, you're going to wind up with a lot of
companies saying, you know, I'm not going to put
anything in because that's a path of less resistance
is when somebody asks me, you know, why is the
facilities expense going to go down 20 percent. I am
not going to be able to prove that it will be 20. One
case it was 15, one case it was 25, you know, I made a
judgment, so -- so that would be my third -- my first
suggestion.
So sort of in -- in summary, you know, I think
streamlining 305 and streamlining 804 will make the
playing field more level. I agree with -- with Matt
that there will be times where it would be easier for
competitors of mine who are, you know, multi billion
dollar companies, they could do an acquisition easier
than me, and private companies don't need the
financials. But, you know, I'd still say, you know,
it's worth it to -- to just make it easier so that
we -- you know, we have at least a fighting chance. I
realize many smaller reporting companies don't have the
recourses or the patience to deal with these rules, but
some do. And, again, I think we're probably an example
of somebody who's -- who's dealt with the rules as they
are and we've still managed to -- to figure out how to
do it. And if you can make it a little bit less
onerous, I think that would be good for -- for all our
investors as well as for the -- for the companies that
we might -- that we might buy.
Yeah, I think the focus on how do I give the
analyst, how do I give the investor the information
they need, you know, that's -- that's the end reason.
I mean, that's all -- the only reason anybody actually
wants to see these financials is so that they can
project forward. Nobody actually cares the company
that you're buying or how much did it lose last year.
You know, that's -- you know, investors assume you've
sort of factored that into the price and you've figured
this out, but focusing on the end result is -- is good.
And, again, if you could figure out how to not require
that repeated consent, repeated management rep letter,
that -- that would make it a lot easier, and then you
could leave it out there for two years. That's, you
know, not a problem.
And so, you know, I -- I echo that the -- that the
suggestions that have been put forth by the SEC are
good proposals. If you don't take any of my advice,
things are still better than they -- than they are
today, but I think there's probably a few things we
could do that could make it just a little bit better
for -- for everybody. And I appreciate everyone
listening to us, and -- and taking our suggestions.
CARLA GARRET: Thank you very much. We
appreciate that.
Do any of the members like to speak?
SARA HANKS: Just --
CARLA GARRET: Yes.
SARA HANKS: I just have a quick question because
we've just been focusing here about -- on the public
companies, and as I understand it, these -- these
rules would affect Reg A companies, right, who would
just follow the -- the rules of the smaller reporting
companies.

I -- I think it would be great if Reg A companies
could get a bit more of a break. I've been in a
situation where we were following the -- the proforma
rules for an acquisition, and when you have an
acquisition of -- by a very small company of an even
smaller company, the proformas just -- it's just
fantasy, and after you've gone through a couple of
rounds of comments, and going -- and fine tune the
elim -- the eliminations, I don't -- really don't think
it adds anything. All it adds is an enormous bill from
the -- from the accountants, and so in my personal
experience we took a bill that would have been X, and
ended up being 2X because of the proformas, which is a
lot for a small company, so different treatment than
smaller reporting companies might be warranted there.
MATT SWARTZ: I think -- I think Bill and I both
agree that that's absolutely right.
BILL KORN: Yeah.
JASON SEATS: I have a stupid question.
BILL KORN: Do ya? Well, we'll probably have
stupid answers for you.
JASON SEATS: Yeah, so first of all, that was an
awesome walk through. That was fantastic. I don't --
I guess -- and maybe this might not even before you
all, but I don't know that I understand how the
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| 1. revenue test or income test is not fully redundant to take a little bit of a balance. Okay. I got to
| the investment test. Like what -- in what cases would protect the acquirer, the -- the company. I do have
| the investment test alone not serve the purpose? protect the current investors, I do have to protect
| BILL KORN: Yeah, so -- so today, at least in our the -- the potential investor who is weighing whether
| situation, there are times, again, when -- when my -- this makes sense. You know, maybe I even have to
| when my income has been pretty close to zero, so the protect the -- the seller in one perspective. So I
| answer is -- did try to sort of balance it and not go all the
| JASON SEATS: Income I get. Revenue I am -- way and say, oh, let's eliminate revenue and income. But
| BILL KORN: -- I am buying -- I am buying you're right, there are certainly situations where
| somebody for zero, it's -- it's actually still something reaches the significance test in terms of
| relevant because if I have $1 either way, the thing revenue, but it's not really significant.
| has reached significance. And, you know, there --
| JASON SEATS: And revenue and --
| BILL KORN: -- are times, you know, that --
| that -- and I -- I would agree they are from a and revenue and --
| shareholder's point of view. How much am I paying for
tests, that it doesn't meet the -- the investment
| this company, you know, that probably makes more of
test, that it doesn't really matter at all.
| a -- a difference. I guess I'll -- I'll give people
| the benefit of the doubt that says if -- when you're
| finished with this acquisition, if you're going to
double the size of the business, I would kind of like
| to know about it.
| And, again, our threshold right now is 20 percent.
| Sometimes 20 percent for a small company means I just
| signed up one big customer. Well, that didn't need all
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| 1. of this work, but, you know, now I've bought a little point, and I think it's probably, you know, one of --
| 2. company that had that big customer. Now it does, so, one of the things that actually speaks to accounting
| you know, certainly you could -- you could argue as a whole, you know, in other words, does -- does --
| that -- that it doesn't meet the -- the investment does accounting for a software company, is it actually
| test, that it doesn't really matter at all. comparable to that of a hospital system or a
| JASON SEATS: The reason why I am asking the marketplace business. In other words, I think
| question too is when I think about different business that's -- that is an issue, and you raise it well.
| models, like you're moving up the li -- you know, It's an issue that transcends even this rule.
| higher up the financial statement, which is -- makes CARLA GARRET: Thank you.
| 10. it easier, but a marketplace business where 95 percent JEFFREY SOLOMON: Yeah, obviously, you know,
| of the revenue doesn't flow to the next line is very again having done a lot of acquisitions like -- like
| different than an enterprise software company where Bill, you know, the -- the tests are actually quite
| 13. 85 percent of their rev -- top-end revenue goes to the complicated. Oftentimes we -- we have a whole team
| next line. And -- and you could end up with the exact that just sits around and does the tests, and --
| same issue with small denominators with the revenue -- and -- and then we try to decide whether or not we
| a revenue test, and you're going to be parsing the think it's significant or not. The -- rather than
| definition of revenue versus like what -- is it a sort of think about -- there's a -- when you look at
| material transaction or not from a market cap the three tests it's because the rule, in my
| standpoint, right? opinion -- it's because the rule has to encompass all
| BILL KORN: I mean, again, I didn't take the -- I different industries.
| 20. thought about this, but I didn't take the philosophy UNIDENTIFIED SPEAKER: Uh-huh.
| 22. that says the -- the easier you can make it the better JEFFREY SOLOMON: But that's -- I mean, that's
| 23. because from the acquirer, that's probably true. I sort of the basic premise on it. The changing to
| 24. mean, if you had no requirement, that would be really market capitalization from assets is -- is actually I
| 25. easy. And if it was -- you know, but I did try to think a reflection of the fact that market
capitalization is a normalizer, you know, companies can be asset light and then they trip up the rules, or other -- you can acquire a business that's asset heavy, and all of a sudden that runs. So market capitalization I just think when you think about the rule changes, it's a much better mechanism for most companies because it's agno -- it's industry agnostic. But I -- I don't think we should be -- I mean, personally I don't -- you know, I don't think that was a stupid question at all. I will just say to you, the amount of work that we do every time we do an acquisition to figure out which tests we might get -- we might have to do it might have to follow is not a inconsequential effort on our part. And we have an entire accounting policy team that just deals with stuff like this.

If you look at what -- what the other revisions are, though, I think the idea of, you know, sort of let's assume that companies for a second are going to be doing things that more oftentimes not are actually going to be significant like, you know, it's not oftentimes that companies are doing a bunch of insignificant acquisitions.

So the -- what I like about what's being done here is it's really looking at how to streamline that process. I will tell you, there's a -- the asymmetry -- and I think you guys outlined it quite well, there's an asymmetry here between private equity and public buyers, and that's actually what this is meant to try and normalize that.

Private equity buyers don't really care about these -- these rules at all, so as a result they become more competitive. When you're a seller, if there's a bunch of work that you have to do in order to comply with being public, it's a cost to you, significant cost to you, or it's a cost to the acquirer, one or the other. That doesn't exist if private equity is actually consolidating. And so I think the premise here we are to consider is that this -- these rule changes are meant to make it easier for public companies to compete with the private equity bid, and -- and while we can't exactly get away from the significant tests, and nor should we, I think we can streamline that process to make it less onerous on the acquirers and therefore the -- the sellers, if you will, or the small businesses that are being acquired can run a more competitive process. That just is taking a step back and saying, Why are we even discussing this. And I -- I don't mean to put words in -- in your mouth. It -- in, you know, corporation finance that, that's my assessment. Am I wrong about that?

William Hinman: No, that's absolutely right.

Jeffrey Solomon: Right.

William Hinman: A private equity buyer is always going to be able to put a ton of people into that other company and do a lot of diligence and see a lot of numbers, manage projections and things that we don't in the pri -- in the public sphere ask for, right? So there's always a -- a little bit of a difference. And what we're trying to do, as you said, Jeff, is reduce the public burden so it's sensible.

So going back three years we didn't think made a lot of sense. We were limiting to two. Making a significance test have fewer anomalous results is, you know, again, one of the ideas.

Your question is a good one in terms of is there a redundancy between some of these tests. We have three. Do we need three? I mean, folks have commented more about the investment tests versus the asset test. You know, those are both measures of how big is this.

The income tests are -- has its own, you know, value, I think. There are situations where you don't pay much for a company, but you're taking on the big operation just because of its loss history or something, so it makes sense to have more than one test, but do we need all three, that's something that people have been commenting on and -- and asking specifically about investment versus asset test.

But we are trying to -- to make them a little bit more streamlined. Some of the points Bill has mentioned in terms of the -- the diligence and the consent process, that's not something in our rules actually required, you know, in terms of getting those -- that diligence done through a comfort letter. That's something for the private sector to sort of work out with the auditors, you know, what can you comfort and what can't you, but we do recognize that when we do ask you to put something in a registration statement, there are generally going to be comfort consequences.

We take this seriously.

Just to kind of go through the rule a little bit more in terms of some of the points you raise. The carve-up financial option is there, it's being broadened. And you said you encourage folks to use it when --
WILLIAM HINMAN: Right. We're trying to be more liberal in
accounted for separately as a segment or as another
particularly if the assets you're buying hadn't been
situations where a carve out will be acceptable,
These are highly technical rules, so you've got to get
due to the carve-out financial option.

WILLIAM HINMAN: Right.
BILL KORN: But to me when it's an asset deal
maybe you don't actually need all those components.
You really need -- here's what I bought, and so now
I've got a statement of assets acquired and liability
assumed, and it's not a balance sheet that balances,
and there isn't a cash flow, and there isn't a
statement of equity, but you know what, you weren't
buying any of that anyway. So if there was a way to
do that, to me I think that would be --

WILLIAM HINMAN: Well, we are broadening what's
there now in terms of the carve-out financial option.
These are highly technical rules, so you've got to get
into the weeds, but you can -- there will be more
situations where a carve out will be acceptable,
particularly if the assets you're buying hadn't been
accounted for separately as a segment or as another
line of business. We're trying to be more liberal in

BILL KORN: When I've done it they wound up
you know, whatever is less significant, that's the number you use, so I think that
works the way you want it to.

WILLIAM HINMAN: Right. I mean, I -- I would say that
the -- sometimes the only way you really ever know how
to do the income piece is if you actually finished
gaining financials ordered because you could sort of
take what the -- what the seller said, but they
don't really done the impairment, they haven't
done -- and so by -- by the time you actually do it,
and in some ways, if you say I'm going to take the
smaller of the two results, you know, you could sort
of say as long as I don't pass -- as long as I don't
trigger the -- the revenue threshold I don't need to
worry, but then the question might be under 804 under
the small business version, do you just eliminate the
whole income question completely? Maybe that's a --

WILLIAM HINMAN: Right. I take your point. It's
sometimes hard to figure out what the income is until
the auditors have been in there for a while, so that's
a fair point.

You had talked about using a pre tax, you know,
number adjusted for extraordinary items versus just net
income in some of these measures. That's a really
interesting thing for us to get feedback on in that
what we were trying to do with the income test was use
an easy to calculate number, and one you didn't have to
go up and sort of, you know, figure out what's an
extraordinary item, adjust for taxes, adjust for
different items. We're trying to use a number that
might be off the face of the financials on the theory
that that may be easier, but if -- if folks who are
going to actually use these rules think it's better to
go up, you know, the income statement a little bit
because that's a more reliable number and a more
meaningful number, yeah, that's a great comment to
make, so --

BILL KORN: Yeah, and especially on -- when --
when I am thinking about the seller's financials.
Because, again, there's -- you know, there -- there
are these one-time non cash expenses, you know,
that --

WILLIAM HINMAN: Right.
BILL KORN: -- something was acquired for 10
million, and it was now sold for 2 million. 8 million
is going to get written off. At some point 8 million

is going to run through the income statement, but it
doesn't really matter. I mean, in some respects you'd
say, Let's -- let's not even figure out whether that
happened two years ago or last year because -- because
the timing of what had happened determines whether
you'll hit the significance test. Let's just say
it's -- it's not relevant. It was no cash -- it was
non recurring. It doesn't affect the people in the
future anyway.

WILLIAM HINMAN: Correct.
CARLA GARRET: I think Burt had some statements
that you've been trying to say.
ROBERT FOX: Well, I mean, a number of -- a
number of comments and a couple of -- of comments as
well. I mean, a couple of recommendations.
You -- first I think the number of tests is
clearly needed. I mean, just the -- you know, we could
talk about the different ones, but some of the
industries, I mean, you know, if we went to a pure
market cap test, the IT and biotech guys would probably
start screaming because their -- their lifetime is
buying pre revenue companies and all of a sudden they
start getting thresholds, right, or limited revenue
companies. The -- the comfort letter, though, this
is -- is really significant, right? I mean, I totally
We say, okay, that presentation is practical, it's what you can get, it's what you use to make your investment decision, and we will generally allow those things to go forward. We may ask them to tweak the disclosure a little bit.

ROBERT FOX: And -- and so then to me it's maybe more either educational efforts, but to Bill's point earlier, I go to a lot of accountants, right, and they say, Well, I haven't seen that before, or I don't think the SEC will ever buy that.

WILLIAM HINMAN: Yep.

ROBERT FOX: Or the attorney will say, That's just a waste of time.

WILLIAM HINMAN: Yeah.

ROBERT FOX: And so I am just wondering whether -- whether it's a policy statement you guys put out or educational efforts, but I don't think, especially if you get to the smaller end of the capital markets companies are taking much advantage of that, and I don't think that they be -- that there's enough belief --

WILLIAM HINMAN: Yeah.

ROBERT FOX: -- that you're going to actually honor a lot of those relief requests.

WILLIAM HINMAN: Again, it's -- it's a very good point.

We, for the last couple years, have been publicizing 313.

WILLIAM HINMAN: You know, because it's sort of an insider baseball kind of rule, and not everyone knows what you need to do, so we've been doing a few things, we've been turning the -- the turnaround time is a lot faster right now. We put out numbers for the staff pe -- person that you called depending on the area where you do need relief, so with phone numbers that will get directed more quickly into where you need it. And we are considering putting out more of what we've done in the past in this area. It's a little bit hard because they are always so fact specific.

ROBERT FOX: Uh-huh.

WILLIAM HINMAN: But we're trying to get people more guidance. My chief accountant is out there.

Every time he speaks he talks about the 313 process and trying to make people more aware of it.

We're also suggesting that you don't need to do the 30-page treatise with your auditor to come in and see us. Give us a two-page outline of what you're thinking about, and we'll give you an idea of whether it makes sense to, you know, entertain that further,
and we will act quickly. So trying to save people
money and act more quickly, but I totally take your
point --
ROBERT FOX: Yeah.
WILLIAM HINMAN: -- that we need to keep putting
that out there and telling people that that's
available.
ROBERT FOX: And I think, Bill, this was getting
to your -- to your carve-out comments as well,
correct?
BILL KORN: Right. Yeah. And I think, again,
you know, our experience is that once we've actually
convinced an auditor that it -- yes, it is
permissible, they may never have seen it. You know,
that was easier, but I'd love to figure out a way to
carve out and just carve out what you bought.
Sometimes you -- you know, what we've done is we've
gotten it better because it was -- you know, it was
part of a bigger business, but we've still spent a lot
of time on -- on things that we didn't really buy that
at the end of the day don't really have the relevance.
WILLIAM HINMAN: Yeah, really the proposal on
carve outs and broadening the ability to use them is
really generated by the work we've been doing on --
ROBERT FOX: On 313, yeah.

WILLIAM HINMAN: -- an ad hoc basis. We're
trying to quantify a little bit of that in the rule,
so that's where that all comes from.
JEFFREY SOLOMON: So the other rule changes I
thought that you put in in terms of shortening the
amount of time you get to go backwards in terms of
doing quarterlies, that's -- that's actually super
helpful just to give you some long feedback. I mean,
when we did our -- we did fairly meaningful
acquisition a year ago that we got at a bargain
discount, so it was actually a discount purchase price
and didn't meet a lot of the same tests, but from an
asset standpoint we felt we had to do it. And it was
a business that was owned by a private equity.
Interestingly enough, private equity didn't do
anything in that business to actually make it ready to
be public.
WILLIAM HINMAN: Right.
JEFFREY SOLOMON: When we got into it, we -- we
basically had a huge argument with them about having
to go back and do three years of quarterly because it
was seemed to be significant we had to show proformas
of our own going back three years, and we had a huge
argument with the seller about what they would have to
do in order to make it compliant. And what it
ultimately came down to is we couldn't close on the
transaction until they completed that work because
we -- we didn't want to be in a position where we
found ourselves "and by the way, three years ago this
business didn't look anything like what it looks like
or" --
WILLIAM HINMAN: Right.
JEFFREY SOLOMON: -- or the business that we
ended up buying, so it was simply, you know, taking in
time.
So I think shortening it up certainly is -- is --
is a very helpful thing. And I didn't even learn this
exemption. I mean, maybe our team did, but I'll tell
you where -- where we've even, we get advice that's,
um, I've got to stop and think about it, so just to be
candid.
You know, you're going -- we're taking that advice
from our auditors all the time on what -- what they
think the SEC will want to see. So in many instances
the advice that we're getting is -- is -- is
prophylactic advice. Like you don't want to get an SEC
comment letter, so here's what you need to do. And
that -- that -- of course when I hear that, and I was a
CEO or CFO here is what they are like, Okay, well,
we're going to jump through all those hoops because we
don't want to get an SEC comment letter.
And the amount of money that we spend to hopefully
not get an SEC comment letter is significant. And so I
just think anything that you can be doing around some
of this you just mentioned is hugely helpful to us
because then we can point to it in the public domain
and say, See, here's an exemption or a place where we
can go. It's not clear to me that our auditors, it's
in their best interest to sort of give us that advice
on how to streamline the likelihood of getting an SEC
comment letter. They make a lot of money at it, you
know, and -- and I am not -- I love my auditors, but I
am -- they are in business too, right? And so I just
think -- that will be really helpful.
CARLA GARRET: Brian?
BRIAN LEVEY: As part of the public company,
smaller public company that's not yet GAP profitable,
very much welcome that the revenue test, and certainly
the market cap test is a step in the right direction.
And to Matthew's point, I think it makes the smaller
companies more competitive with the bigger companies.
I did M&A and eBay for 13 years, and we never had to
deal with these issues, and so there was a ton of deal
certainty that we've had to look at a lot more lately
to the extent we want to be inquisitive.
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<td>The one area that I thought didn't add to support or we don't, you know, but voting on whether we streamline things was the synergies disclosure, especially for smaller companies, where it seems like to support the -- the proposal to amend these it's very much up for judgment, we're going to be taking longer to work with the accountants and the auditors on the financials, there could be a release of sensitive disclosures. It just seems very open to discretion. And looking at some of the comment letters from folks that, you know, I have worked with before and trust that, you know, I would just -- I don't want to come up with a recommendation? Are we -- is there -- recommendation?</td>
<td>support or we don't, you know, but voting on whether we do support the -- the proposal to amend these requirements, we could make it where they were subject to, but we could say we do support the new revenue test, we do support having that fair market value as the denominator in the investment test.</td>
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<td>CARLA GARRET: Thank you, Brian. I would actually add on that. I was general counsel of a -- a smaller reporting company, and we did -- we acquired a lot of companies, and -- and that -- that last column would have scared me to death as a general counsel, and I probably would have -- not only from the sake of our perspective, which I appreciate you clarifying that that would be, you know, subject to safe harbors, but from a -- a really -- a</td>
<td>Does anybody have anything else to say before I come up with a recommendation? Are we -- is there -- are there any subjects that you'd like to put in the recommendation?</td>
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<td>CARLA GARRET: Right. I mean, that would be a hard thing to get comfort on, so I was concerned about that too. I -- I love the revenue test, I love, you know, the new denominator for the fair market value, I love the shorter periods of time. I -- I don't know how many other people want to talk about issues in particular or we now would like to -- to come up with some recommendations with respect to saying that we know, I think Burt's right. I don't think Burt -- I</td>
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<td>target company disclosing outright, you know, which facilities are going to close, how many employees are going to be laid off, some of that information you might think is going to happen at the beginning, but then when the acquisition actually takes place you close the deal and you realize actually that's not going to -- we don't need to do that, and so -- but you have disclosed that in a public document. I'm just taking a step back and saying as a general counsel of a public company, I would highly recommend my client to be very, very conservative in terms of what I would have disclosed in that column, and especially -- you're not going to give us comfort on that, so --</td>
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<td>ROBERT FOX: Nope, at least not unless the stand changed, yeah. CARLA GARRET: Right. I mean, that would be a hard thing to get comfort on, so I was concerned about that too.</td>
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<td>JEFFREY SOLOMON: Yeah. can -- can we spend two seconds on that because I'd be curious to hear -- you know, I think Burt's right. I don't think Burt -- I</td>
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<td>SARA HANKS: Just subject to Reg A.</td>
<td>SARA HANKS: Some kind of flexibility.</td>
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<td>SARA HANKS: Subject to Reg A.</td>
<td>CARLA GARRET: And Greg?</td>
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<td>SARA HANKS: Yeah.</td>
<td>GREG DEAN: And then some -- some potential tweaks or modifications on the -- the synergies of management adjustments piece just to -- to make it easier on small business, and so that I'm not frightened to enter into any M&amp;A.</td>
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<td>JEFFREY SOLOMON: Right.</td>
<td>JEFFREY SOLOMON: Uh-huh.</td>
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<td>CARLA GARRET: You know, because I think you have to have fact-based certainty, right?</td>
<td>ROBERT FOX: You know, because I think you have to have fact-based certainty, right?</td>
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<td>SARA HANKS: May I?</td>
<td>JEFFREY SOLOMON: Right.</td>
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<td>CARLA GARRET: Yes, Sara.</td>
<td>ROBERT FOX: And you don't have it, right? And the points have already been made. But, yeah, I mean, I think -- you know, we raised it, my firm in our comment letter and all the other firms, right, that at least the way the current standards read and the way the liability structure is I just don't imagine -- you know, I mean, there's really two-fold, right? You'd have to have a change in the standards first, and then secondly even then we'd have to then get comfortable with having your factually adjustable, right?</td>
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<td>SARA HANKS: And Greg?</td>
<td>ROBERT FOX: And you don't have it, right? And</td>
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say from -- from -- I'll speak from first the CEO's
perspective, but then I'll speak from an investor's
perspective because I spent a lot of time being an
investor. So first I didn't care -- you know, as an
investor -- I'll speak as an investor, I don't care if
you got a comfort letter or not. I'm interested
actually to know what management thinks because I am
going to hold them accountable, right? So show me
what you think the proforma is likely to look like. I
mean, research analysts that actually -- right, will
use that and then they'll make their own
interpretations on whether or not they think you can
achieve the synergies or whether or not the proformas
will work. That's actually the job of a research
analyst is to take what management says and say, I
agree with it, or I don't agree with it, or here's
where the risk is in this assessment. And so to me
that's a very valuable communication tool post
acquisition that the comfort letter is irrelevant for
that. I'm not looking for comfort from an auditor on
that, I just want to know what management thinks, and
I want to hear what the research analysts and other
people who cover the stock think, and that gives
management a chance to say, This is what we think, and
you can hold us accountable to this. I will say
whenever we do our proformas, that's where we spend
most of our time with investors frankly.
Again, speaking now as a CEO, we spend a lot of
time with investors on our proformas trying to -- it's
a chance for us to say this is what we think will
happen, and then if we don't deliver on that,
obviously, you know, we have to be held accountable.
But, again, all of that happens outside of the scope
of -- of needing to get comfort because it's really
just management's point of view. And so that would be
very -- I think a very helpful tool to -- to get some
guidance around not having to have comfort in those
because it gives us a chance to present our case. And
then when you think about all of the conference calls
and everything we do afterwards, it's clearly
highlighted as management's point of view, it's outside
of the accounting scope, and then we can have a much
more substantive conversation with our investors so
they can, you know, choose to, you know, model it up or
do whatever.
WILLIAM HINMAN: So --
JEFFREY SOLOMON: Does that make sense?
CARLA GARRET: Yes.
JEFFREY SOLOMON: But -- but is that kind of more
of an argument, though, that it shouldn't be in the
registration statement itself, and should be allowed
kind of what's going on now, which -- which I think is
the issue you're trying to address, right, is that
necessarily small businesses, but a lot of companies
go out and they do a road show and they -- they talk
about this stuff, right? It's in their analyst
presentation and they talk about it, but it's not in
the registration statement itself, but I think -- you
know, don't you run a risk that if it's there, there
may be a -- there may be an expectations gap of -- of
what has been, you know, verified or not?
WILLIAM HINMAN: Sure I mean today as mentioned
it's these numbers are often the nicer -- the better
of synergies are discussed at length on the road show
JEFFREY SOLOMON: Uh-huh
WILLIAM HINMAN: The full picture may get some
mention along the way, and it's not in the
registration statement We certainly take the point
that it's the kind of thing that auditors historically
have not given comfort on or, you know, you wouldn't
think it would be very hard to get comfort on. Our
rules don't require comfort per se, they require due
diligence. You want to have due diligence defense,
one of the things you can do is to have a comfort
letter. There's other ways to diligence numbers where
you can do your own work and think about this if
you're underwriting that deal or if you're involved in
that transaction, and you would have wanted a comfort
letter, but you don't get it, you do substitute
diligence.
So the comfort letter point we'd certainly take,
it's -- it's a good one. By requiring people to put
those management adjustments in the book they are
standing a little bit more firmly behind them. There's
a different level of liability, and so the question is,
is that useful?
We're asked -- you know, we've talked about this
as something that would be required when either
reasonably certain, some commentators have suggested that
these should be optional. That might be another way to
go, you would see people putting -- putting them in
when they thought they were fair, a fair presentation
and were comfortable with them.
JEFFREY SOLOMON: Uh-huh.
WILLIAM HINMAN: And everybody from a diligence
point got comfortable with them, and you'd see that
for that deal, and you'd see other deals that have
been left out, and that may give you a better idea of
what -- how firmly management believes in those
synergies.
JEFFREY SOLOMON: That --
WILLIAM HINMAN: So that -- that's a comment, you know, we were receiving, that's another comment people could make. Right now it's proposed as a -- as a requirement, but that doesn't mean that you can't comment otherwise.
JASON SEATS: If -- if the requirement, though -- if the goal is to try to equal the playing field to a private equity buyer, private equity buyer is not required to make those filings, and so you get that it might be the same analysis they would be doing, but I don't -- it's -- it's a --
WILLIAM HINMAN: Well, in some ways we would be leveling the playing field because a private equity buyer certainly does take those synergies into account.
JASON SEATS: Of course.
WILLIAM HINMAN: And that's one of the things that --
JASON SEATS: And there's no reason that a public buyer would not also be doing that behind closed doors, right?
WILLIAM HINMAN: If they don't have --
JEFFREY SOLOMON: Except they can't get access to it.

WILLIAM HINMAN: Do they have the information, and is it as reliable as you'd want it to be?
JEFFREY SOLOMON: So a public investor can't get material non-public information, right? That's the thing, is how does the information get into the public's hands, right? So if you think about it's really private equity versus public equity, right?
And private equity has when it does its acquisitions it does the same due diligence, it just doesn't have a disclosure, it's consuming it for itself.
Public equity, there's no way for a public company to get that information into the public domain so you can actually have a conversation about it, and you then now you're -- you're on Reg FD and a bunch of other things where how do you talk about what your synergies are if you don't have a public document to actually talk about it. And if you have one-on-one conversations with public investors in about -- in something that's not disclosed in an 8-K or then all of a sudden you're -- there's an 8 -- you know, now you're running afoul some real serious problems.
WILLIAM HINMAN: Well, folks --
JEFFREY SOLOMON: So I think this is about how to get that.
WILLIAM HINMAN: Just to be clear, when folks do this in an M&A context, they go on a road show, those road show materials are required to be furnished to the SEC, but there's a different standard of liability.
JEFFREY SOLOMON: Yeah.
WILLIAM HINMAN: It's not in a registration statement per se.
JEFFREY SOLOMON: Right, so we -- we've actually completed two things. I wasn't thinking about it from a registration standpoint. I mean, it would be if you're doing financing alongside of an acquisition.
WILLIAM HINMAN: Right.
JEFFREY SOLOMON: That's for sure. I just, you know, when --
WILLIAM HINMAN: Which is the only time you'd have a comfort.
JEFFREY SOLOMON: Right, you would be talking about an 8-K filing here where you're essentially doing pro forma financials, which is essentially what -- it depends to your prior registration statement if you had any outstanding or your -- your public filings.
And I -- I agree with you by the way. So there's another thing to consider here --
CARLA GARRET: Question?

ELAD L. ROISMAN: I'd rather hear from you, so --
JEFFREY SOLOMON: Oh, sorry. I -- I think it's actually -- from an investment banking standpoint, certainly fairness opinions can deal with a lot of the issues, you know, and -- and there when you're hiring a financial adviser like an investment bank, that investment bank can actually provide a fairness opinion. It's not the same things as a comfort letter, but it's an opinion that, you know, oftentimes goes along with a meaningful acquisition to the public. And there, I think that that -- you know, if there's some guidance around what -- what's allowed to be put into the management, what's -- what's allowed to be put into these pro forma financials.
As an investment bank we -- we would take that under advisement and help to craft that and be able to say, you know, these are things -- well, based on our diligence as part of the fairness of being in process that we think are eminently achievable. It's a different level of --
WILLIAM HINMAN: Yeah, you'd have to do your own diligence.
JEFFREY SOLOMON: But -- but at least you have a financial intermediary in there who is, as part of the
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<td>1. fairness opinion, deliverable and say, you know, this seems reasonable or fair.</td>
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<td>2. Sorry.</td>
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<td>3. ELAD L. ROISMAN: No, no, like this has been great. I like what I'm hearing, and I appreciate it.</td>
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<td>4. It's like, you know, you saw what we were trying to accomplish was make more proformas more useful and hold issuers accountable for the synergy disclosures.</td>
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<td>5. It just sounds like proformas may be not the most perfect vehicle for communicating synergy, you know, predictions. So you understand what we're trying to achieve and also what you think is achievable. I would like to -- for you guys to think about whether it's there, or later, you know, what is the best way to kind of meet that burden, and to Brian's point, allow you guys to do what you're trying to do, so -- but this has been incredibly helpful.</td>
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<td>BILL KORN: Yeah, I mean one thought maybe that proformas could go in the 8-K, but not necessarily transfer it to that registration statement so that you could do it there without the need for the -- for the comfort and -- you know, and then the -- then when you're doing proformas as part of an S1 or an S3 you include the transaction adjustments, but you don't include the management adjustment cup. So the 8-K could include it, you know, you could give it out to, what, the shareholders, you could actually talk about that on a road show and it would be in the public domain, but you weren't necessarily putting the same level of -- of heft behind it.</td>
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<td>MATT SWARTZ: And just to add to that thought, Bill, to Brian and Carla's point, having served as general counsels of technology companies that are growing, but really any small business. I mean I think the cultural impact of having to publicly talk about what cost savings are going to result from the acquisition is -- is an enormous cultural and -- and real business issue for -- for -- certainly for sellers, but for buyers too. And it's a reality that all buyers are probably looking for synergies and cost savings, but the only ones that have to -- would have to make them public would be public companies. And I think the market in these things in M&amp;As, more often than not I have experienced company owners telling buyers I want you to take care of our people for at least a year. I haven't seen a lot of agreements that go beyond a year, but often that point is specifically negotiated. What happens after a year, I think, you know, there's less control over, but it's -- proforma would be a very serious issue if you had to publicly announce your intentions to synergize employees away.</td>
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<td>CARLA GARRET: I agree with that.</td>
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<td>3. So at this time, let me see if I can summarize a little bit and tell me where I am right and tell me where I'm wrong, but a possible recommendation would be for us to say that the committee supports the commission's proposal to amend the financial reporting requirements for the acquisitions and dispositions of businesses including Rules 305, 314 and Article 11 of Regulation SX subject to the following recommendations, that the Commission continue to look at Reg A companies and them having different treatments under these rules, that the Commission further look at the disclosures of the management discussion, including whether synergies should -- and the proforma column should be mandatory or optional or not included at all.</td>
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<td>4. Any object subject issues?</td>
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<td>5. I think in addition to the revenue test we support the addition of the fair market value for the investment test as a denominator, to support the decrease in the number of years of financial statement from three to two?</td>
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<td>7. CARLA GARRET: Okay. On that what I'll do is call for a vote on what I just stated unless somebody wants me to repeat it.</td>
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<td>8. Is there a motion to approve?</td>
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<td>9. HANK TORBERT: Motion to approve.</td>
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<td>10. CARLA GARRET: Thank you. Is there a second?</td>
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<td>11. WILLIAM HINMAN: Second.</td>
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<td>12. CARLA GARRET: Okay. All in favor of that recommendation?</td>
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<td>13. (Several ayes.)</td>
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<td>14. CARLA GARRET: Okay. Anybody opposed?</td>
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<td>15. (No response.)</td>
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<td>16. CARLA GARRET: Great. We've just passed our first recommendation, and the recommendation has been approved by the committee. And I think we actually finished five minutes early before lunch. And so I want to thank you again to Matt and Bill for joining us here today. Your presentations were excellent, and I think gave the Committee a lot of insight to these matters, so thank you very much.</td>
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<td>BILL KORN: Thanks for inviting us.</td>
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<td>18. MATT SWARTZ: Thank you.</td>
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<td>19. CARLA GARRET: You're welcome. And so what I'll do is I'll adjourn the meeting for lunch, and the meet -- the Committee will reconvene at 1:15. If you're joining via webcast, please note that the</td>
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webcast will be stopped during this period, and that you can rejoin the meeting at 1:15 Central time.

Thank you.

(11:56 a.m. - 1:16 p.m. -
Adjournment while the Committee broke for lunch.)

CARLA GARRET: Welcome back from lunch. I hear - hereby call the meeting back to order. I thank Chairman Clayton and Commissioner Pau who have joined us. Welcome.

CHAIRMAN JAY CLAYTON: Thank you.

CARLA GARRET: And I understand that Chairman Clayton - would you like to talk to the committee?

CHAIRMAN JAY CLAYTON: Oh, okay. Thank you, Carla. I understand these mics are way hot.

Thank - thank you members of the small business capital formation advisory committee, Martha Miller and the staff and Office of the Advocate for Small Business Capital Formation for holding this second meeting of the Committee outside of Washington, DC.

This demonstrates a clear commitment to capital formation across the country. I thankfully -- I thank you for your thoughtful and pragmatic exploration of how our rules, regulations and policies impact small businesses and their investors including

smaller public companies. In that vein, a very big thank you to Creighton University for the warm welcome to Omaha, Nebraska.

The agenda today is packed with substantive topics that I can -- that I believe can have a very positive impact on smaller companies and their investors. This morning you already heard from the staff and the Division of Corporation Finance about the SEC's concept release on harmonization of securities offerings exemptions.

The concept release is the first step in what we hope will be a much needed form of our exemptive offering framework, which I have referred to before as an elaborate patchwork.

I understand that this morning was also the first step for the work of the committee in this area, and that you will continue to consider how we can harmonize and make more effective our exemptions from registration at a future meeting of the committee.

The opportunity for improvement in this area is stark. Private capital raising is now outpacing capital raising in our public markets, and our main street investors have no effective access to investments.

Further, the availability of private capital is

geographically skewed. And as we discussed at your first meeting, significantly favors companies with values and ex -- valuations in excess of $50 million.

I look forward to your work in this area.

In the meantime, I encourage everyone, including small businesses and their investors to send us their comments and share their suggestions for how we can improve the exemptive offering framework.

This morning you also discussed our proposed amendments to the financial reporting requirements for acquisitions and dispositions of business. I am pleased you are tackling this topic, especially since I realize that it's not an easy one. So let me be clear about what I hope we can achieve with these amendments.

First and foremost, we need to ensure that investors receive the financial information they need to understand the potential effects of significant acquisitions or dispositions.

Second, I believe we can deliver for investors while eliminating all necessary -- all necessary costs and burdens imposed by the current rules, that in my experience can and do frustrate, and let me emphasize frustrate, attractive acquisitions and dispositions including those involving small businesses.

The proposed rules reflect the experience of the

staff and the Division of Corporation Finance gained through years of working with these rules. I commend them for their world.

The last topic on your agenda today is also a direct result of the efforts of the Karun staff.

Bill, you and your staff have been busy. In May the SEC proposed amendments to more appropriately tailor the accelerated and large accelerated filer definitions. Under the proposed amendments smaller reporting companies with less than 100 million in revenues would not be required to obtain an attestation of their internal control over financial reporting.

They refer to it as ICFR, for an independent outside auditor.

Importantly, the proposed amendments would not change key investors protections from the Sarbanes-Oxley Act of 2002, such as independent audit committees, CEO and CFO certifications of financial reports, or the requirement that companies continue to establish, maintain and assess the effectiveness of their ICFR. And, of course, the financial statements of those companies would continue to be audited by an independent outside auditor.

What the proposed rules would do is allow these lower revenue companies, many of which are biotech and
healthcare companies and their investors to benefit for more tailored control requirements, so they will be able to redirect savings in growing their companies. We are not proposing these changes in isolation. We are building from the experience we have gained since the Jobs Act of 2012 exempted companies with less than 1 billion in annual gross revenues from the ICFR attestation requirements during the first five years following their IPOs. In many cases -- and this is important and has not been emphasized enough. The proposed rules would simply extend this widely lotted Jobs Act exemption beyond the five-year window for companies that have not achieved more than 100 million in revenues. I look forward to your discussion this afternoon. Thank you.

CARLA GARRET: Thank you, Commissioner Purse.

COMMISSIONER PURSE: Thanks, Carla. And thanks to all of you for being here today, for making the trip out here to Omaha, and I am really delighted that we are meeting somewhere outside of Washington, DC. I always highlight the importance of thinking about capital formation from the perspective that's not just focused on the coast, but it's focused on the Heartland of the countries, where I am from as well.

I am not from Om -- from Omaha, but I am from Ohio, so there are a lot of similarities. I want to thank Martha and her office for putting this together, and just sorry that I wasn't able to be here this morning for the discussion. It sounds like it was a very interesting and lively discussion this morning. I am very much looking forward to this afternoon's discussion. I think as the Chairman highlighted, we're really trying to get the balance right and making sure that investors get the information that they need, but not -- not imposing costs on capital formation that prevent transactions from occurring that -- that would happen in the absence of -- of those regulatory burdens. And so trying to get that balance right is very important to us, and I think you all are really key to helping us figure out how to get that balance right, so I look forward to hearing what you have to say this afternoon. Thank you.

CARLA GARRET: Thank you, Commissioner Purse.

COMMISSIONER ROISMAN: Thank you, Commissioner Purse.

ELAD L. ROISMAN: Yes. Well, thank you again everybody for coming here to Omaha and to Creighton University. Thank you, Creighton University, for allowing us your space and your time and all your assistance. It's great to be here in Omaha. As much as I enjoy our meetings in the windowless basement of the SEC, the change of scenery is much appreciated.

So I -- as you can probably tell, I have been looking forward to this meeting since last May, since your inaugural one where I was -- I was president. I thoroughly enjoyed that first meeting. It's -- I remember being so impressed by your enthusiasm, your camaraderie and participation on a lot of really substantive matters, and I look forward to continuing that. It's already begun this morning, and into future meetings.

I'll say you guys have set a really high bar for yourselves, but I think you guys will -- will need it. I took a lot of notes during today's discussion, both on the harmonization concept release and the -- the proposal to amend the financial disclosures for acquisitions and dispositions. I think it has given us a lot to think about, which we'll take back to Washington, and I very much look forward to continuing that into the next topic, which is the proposal to amend the accelerated and large accelerated filer definition.

So when this was proposed, I gave remarks and I noted that it was -- the proposal we had was well supported by the economic analysis provided. With that said, I think my question to you and to everyone else is there different or more recent data that we did not take into account that would support explaining relief to appropriate issuers. And I think that's a question where your input would also be particularly helpful.

I would also be interested in hearing the proposed definitions will introduce complexity to small businesses trying to figure it out. We even kind of talked about that earlier today, but I think that's really helpful, and a lot of you noted that you'll go to sophisticated counsel or accountants or auditors -- auditors to figure that out, is there a way for us to potentially simplify that.

So in closing I really thank you guys for your dedication and perspective that you provide the commission. Thank you to today's speakers, you know, your knowledge and insight on these particular issues is not only incredibly helpful to everyone here, but to everyone listening and watching and to the staff back in the home office who is working with us. You know, I realize you have day jobs and you're traveling here, which makes it a little harder, but we really do appreciate it.
And lastly, but definitely not least, thank you to Martha Legg Miller, Julie Davis, Jenny Riegel and the Office of Small Business Advocates. You guys have done a tremendous job, and I look forward to the continued work that you will do.

CARLA GARRETT: Thank you. Thank you, Chairman. Thank you, Commissioners.

Our next agenda item is the SEC proposal to amend the accelerated and large accelerated filer definitions. And, Jeff, our vice chair, is going to introduce this topic.

JEFFREY SOLOMON: Thanks, Carla. And I hope I do as a masterful job as you did this morning, so -- probably won't, but it's -- it's a high bar.

Thanks to the Commissioners and to the staff for -- for making this easy for us. We actually do have day jobs, you're right about that. And -- and so any time you get called on to be able to participate in a public discourse around things that are really critical to the economic health of the country, it's an honor and a privilege, so thank you for giving us the opportunity and using your power to convene to do something I think we all think in this committee is extremely constructive.

I'll just say before we get started, one of the things that in discussing all these topics, and in actually reaching out to a number of people to participate, it's given me a chance to articulate what the role of this committee is. And the feedback I've gotten almost uni -- unilaterally from companies and from investors has been, Wow, I had no idea that the SEC was actually so integrally involved in something so important. And it's really a great example of how -- I mean, how -- how government involvement can be extremely constructive around topics, and so I think, you know, you should just know that I think part of our responsibility in this committee is to communicate that more broadly. The fact that we're in Omaha today and tomorrow I think is indicative of really -- of the -- of the impact that we can potentially have beyond the coasts, and that's as you and I have discussed from being from the Midwest is pretty -- pretty critical, so --

Okay. So just some quick background, we'll get through the -- the detail of it and then we'll open it up for -- for discussion from our speakers.

In June of 2018, the Commission released a proposal to attend the accelerated and large accelerated filers.

Prior to the SRC amendments, non accelerated filers, accredited filers and large accredited filers were those with the same qualification threshold of 75 million of public float as SRCs, and under Sarbanes Oxley, Section 404A, all companies must maintain internal controls over financial reporting or ICFR, which management must access in its periodic reports.

Accelerated and large accelerated filers must also comply with 404B, which requires an additional independent auditor attestation of management's assessment.

Non accelerated filers are exempt from the additional 404B auditor attestation, as are emerging growth companies during their five year on ramp post IPO for the Jobs Act.

So the proposal in May of 2019, is that the Commission released a proposal to attend the accelerated filer and large accelerated filer definitions. The proposed amendments would result in smaller reporting companies with less than 100 million in revenues being non accelerated filers.

The proposal uses a different framework than the updated SRC definition, although both include a test based on company revenue. The proposal is intended to reduce the cost for lower revenue companies while also maintaining your effective investors protections.

So before we get started and I introduce the speakers, we're going to try on the committee to -- to follow the similar format that we did with the second section this morning, which is we're bring the conversation to a close, probably about 15 or 20 minutes before the end.
of our time, and then really try to get together and see if
we can bring about some consensus on -- on making a formal
recommendation. Obviously we will be having many
conversations be -- before then, but the goal would be to be
able to make a formal recommendation at the end of this
session.

So our -- our speakers, I think you met Bill
Hinman and Jennifer Zepralka this morning from the SEC, and
then Charles Crain, who is the director of tax and domestic
economic policy for the National Association of
Manufacturers, which represents 14,000 manufacturing
companies. Charles leads the organization's policy in
advocacy work on corporate governance and financial
services, and his prior experience includes work on the
hill. He's a graduate of Mercer University in Macon,
Georgia.

And David Maley is senior vice president and lead
portfolio manager at Ariel Investments. He runs the funds
micro cap and small cap deep value strategies, and manages
the firm's domestic trading teams and chairs their trade
oversight committee.

I joined the firm in 2009 bringing 25 years of
investment experience as a graduate of the University of
Notre Dame, where he has a BBA in finance, and the
University of Chicago where he has an MBA.

I think you did a really good job, Jeff, of
summarizing what the rule is trying to do, you know, the
perspective of a year ago we changed the universal companies
that would qualify as small reporting companies to include
companies with up to 250 million in market cap or 700
million in market cap if you had less than 100 million of
revenue.

And it used to be if you were qualified as a small
reporting company, you did not have to provide the outside
auditor attestation over your internal controls. When we
changed that rule a year ago, we did not sort of make that
parallel change and say, So long as you're an SRC, you don't
have to provide that attestation. Instead we decided to
look at that a little harder. The chairman at the end of
the rule making, and the rest of the commissioners directed
our division to take a look at the qualifications where the
exemption from the attestation requirements.

At that point, and right now if you're more than
-- have more than 75 million in market cap, you have to
provide that attestation. We were asking ourselves, is that
the best place to draw the line, does that strike the right
cost benefit analysis. Are all companies over 75 million
getting the good -- the investor is getting a good return on
the costs of that exercise, the outside auditor attestation,
or is there another way to kind of describe that universe.

Full disclosure, he is also a Cowan shareholder,
so I just want everyone to know that, so I work for him.
That's pretty much how I view that.

On the phone I think we have Mike Robb. Mike, are
you there?

MIKE ROBB: I am.

JEFFREY SOLOMON: And Mike is the president and
CEO of Ardelyx. Ardelyx is a biopharma company
focused on developing treatments for cardio -- cardio
renal diseases. Mike has experience -- significant
experience as a CEO in the biotech space, and prior to
that was spending 15 years as a venture partner at New
Enterprise Associates, so we -- we really do
appreciate you sharing your perspective, Mike, as
well.

Okay. So let's -- I think I got it all. Did I
get it all there? Great. So let's open up the conversation
and we'll start -- I don't know, Bill and Jennifer, if you
had anything that you wanted to start with, and then
we'll -- we'll work down the line.

WILLIAM HINMAN: Sure. Thanks, Jeff. We'll get
a little bit of more background on the proposed rule.
I'll talk briefly, and then Jennifer will fill in some
details, and then we'll hear from our analyst, whose
perspective I am anxious to hear.

And so the proposed rule does try to have another test,
which is basically a test that you could pass to be an SRC.

You have under 700 million in market cap, and under 100
million in revenue.

If you do, perhaps your financials are less
complex. With that little revenue, there is probably not
complicated rec issues. You may still be in a very early
development stage. You have a higher market cap, but you
have very few revenues. And so you probably are early
stage, and you're probably a kind of company that could
really benefit from investing that money instead of with
your auditors for the outside attestation, perhaps another
clinician or more R&D, whatever it is that is causing that
high-market cap, but low revenue profile. And so we took a
real hard look at that as our colleagues in the division of
economic and risk analysis to see what they thought.

And we think we have the right line there, that if
you're under 100 million in revenue, and 100 -- under 700
million of market cap, perhaps the cost benefit is such that
we don't -- do not require the outside auditor attestation.

We are -- also a question, though, is -- and to
keep things simple, would it be better to say, If you're a
small reporting company, you don't need to prove this
attestation. And so that's a question in the proposal, it's
something we're continuing to consider, people are
commenting on that, we'll be interested in the Committee's views, but so far we have led with the 75 -- excuse me, 100 million of revenue and under -- and under 700 million in market cap.

A couple points that are probably worth emphasizing. Even if the companies that now would qualify for the exemption do not provide the attestation, their auditors when they do the audits still are required under the accounting literature to review the quality of the controls. So it's not like this is a free pass that the controls do not need to pass muster, the auditors will still look at them and take them into account as they structure the audit.

So if the controls are not up to snuff for an attestation, they may not be as systematized at that point. The auditors, we would presume, would be doing more manual checking and make sure that the audit still was done in a responsible way, so it's important. That's, I think, an important point to emphasize.

One of the things that we are interested in the Committee's views and others, is the cost of the attestation. There's been a lot of question around how do you measure these costs of going through the attestation requirement. And there's obviously the additional fees that the auditors may charge, there's additional management time that folks will incur.

And the other thing that's -- I used to see in private practice that -- again, it would be interesting to hear the committee's views and the panelist's views, is that when companies got to that stage where they are thinking of providing the outside attestation, they typically had to go through some systems upgrades. If the auditor was going to attest, the auditor would say, It's time to do an upgrade if you want our attestation. It wasn't that the financials themselves had gotten to a point where they were so complicated that was required, it was because we needed to check the box and add the attestation. If left to their own, the committee -- the company may have decided to do that at a later stage, but not there's a systems upgrade that kind of follows along with this, and that's another cost that we're very cognizant of when we're thinking about requiring outside attestations.

So we are, you know, curious to hear from the committee on having the flexibility to decide when you do those upgrades and whether or not attestation is provided, you know, how useful is that for you, will the money saved by used in the business in other ways that could be productive, or because people have commented on attestations can be good for reducing our cost of capital. We voluntarily do it, but under this proposal what we're suggesting is by lifting the thresholds more companies can make that decision for themselves as opposed to being required to do it through the regulations. That's what this is all about.

That's the broad overview, and those are some of the things that we're thinking about. I'll let Jennifer add a couple of details.

JENNIFER ZEPRALKA: Thank you. I -- you know, I think between Jeff and Bill you've heard now the contours of this -- this proposal that's in -- that's in the release about the -- the exception for small reporting companies that meet the revenue test.

I just wanted to mention before we get into the discussion, there's -- there's some other proposals in there. We are proposing to amend the transition provisions, so this is, you know, a little bit in the weeds, but when you are coming in and out of accelerated or large accelerated filer status there are -- there are tests that you have to look at.

Right now under the existing transition rules, an issuer that is accelerated or large accelerated doesn't fall out of that into non accelerated status until the public float falls below a lower threshold than the one that is required to come into the status. That's intended to keep companies from popping in and out of accelerated filer status just based on minor fluctuations in their -- in their public float.

Under the proposed amendments we -- we're asking to increase the transition thresholds for those -- for accelerated and large accelerated filer for -- from 50 million, and to exit large accelerated filer status from 500 million to 560 million. This would align everything at 80 percent thresholds, which is consistent with the thresholds that are used for SRC, Small Reporting Company Status, and we would want to add the revenue test to transition thresholds for exiting both accelerated and large accelerated filer status, so that an issuer that is accelerated now would remain one unless -- unless either its public float falls below $60 million, or it becomes eligible to use the smaller reporting company accommodations under the revenue test, so it aligns coming out the way we're proposing to have it come in.

Again, it's a little hard to -- to wrap your head around that because it is pretty technical, but I just wanted to -- to mention that that's another part of the proposal.

And then briefly just before we start, the comment period ended on July 29th on this proposal, but you can, of course, still submit comments. We've gotten 62 letters as of yesterday. Many of the comments are supportive of the
proposals, particularly from the biotech industry and some
community banks have been very favorable. Many commenters
have noted the resource constraints for pre revenue and
lower revenue companies that Bill was just talking about,
and note that the resources that go to 404B attestation now
could instead go to expanding their businesses and increased
R&D.

We've also heard support from issuers that are on
the verge of aging out of emerging growth company status and
concerned about the transition to needing to do the auditor
attestation.

A few other commenters are supportive of the
proposals, but suggest we go farther and align the smaller
reporting company and non accelerated filer status so that
all small reporting companies would be non accelerated
filers, and of course there are several commenters that I'm
not saying last because we're not listening to them, but
there are several who are not entirely supportive of this
proposal and who are making sure that we hear their views
about the benefits of the auditor attestation to investors
in small, low revenue companies inciting a need for more
analysis of the costs and benefits of our proposal
And with that, I think we can hear from our
panelists.

JEFFREY SOLOMON: Charles?

Charles Crain: Well, thank you so much, Carla
and Jeff, for having me today, and -- and to Martha
and Julie and -- and Jenny in the Small Business
Office team.

I know Jeff already gave a brief introduction of
me. I am Charles Crain again. I lead our corporate
governance to finish services work at the National
Association of Manufacturers. The NAMM has about 14,000
member companies, member manufacturers in all 50 states,
every industrial sector you can think of underneath that
large manufacturing umbrella. 90 percent of our members are
small and medium sized companies. Looking at the
manufacturing industry nationwide, there are about 250,000
manufacturers. 98 percent of them have fewer than 500
employees.

Do I need to do something?

CARLA GARRET: No.

CHARLES CRAIN: Okay. I have slides theoretically
somewhere, but they are also in your -- I'm sure we'll
send around the materials so I have notes without
that.

Anyway, 98 percent of manufacturers have fewer
than 500 employees, and three-quarters have fewer than 20,
so these are -- these are largely small businesses, and
there are -- these companies make up 64 percent of private

sector R&D spending in the United States, so that I think
relevant to this conversation is a significant outlay, what
do we talk about, what they might -- what else they might be
spending capital on.

There are also 13 million men and women who make
tings in America, and we -- we sort of speak on their
behalf as well.

Manufacturing is a capital-intensive industry, as
I am sure all of you know. Manufacturers turn to the public
markets for financing R&D, for significant equipment
purchases, job creation, business growth, etcetera, and --
and those pro growth activities fuel economic expansion
across the country, and certainly beyond just the coast.

Just here in Nebraska, manufacturing makes up 11 percent of
the state's domestic product, and it employs 100,000 people
just here in the state.

And so when we talk about these issues, about
access to capital, yes, it's obviously very important to
manufacturers who are looking to expand their business, but
it's also important to manufacturing workers. Our industry
is above average in terms of providing retirement benefits
to employees. About two-thirds of manufacturing workers
have a retirement plan through their employer, and, of
course, they are also individuals with their own, you know,
multiple fund retirement account, what have you.

Those workers need companies to go public early in
order to take advantage of the upswing as that company
grows. The company needs to go public early obviously to
fund its growth, to finance its growth on the public market,
but from the workers' perspective, if companies aren't going
public until they have revenues, have a higher public float,
whatever it is, then -- then the workers -- the every day
main stream investors miss out on that -- that growth
opportunity. And unfortunately we can -- we can see that
play out in the economy.

Over the last 20 years the number of public
companies in the US has been cut in half, and they are much
larger companies. In 1996, the average market cap of a
public company was $1.8 million, today it's $7.3 million, so
that's a more than three-fold increase in the size of
company, and that issue starts at IPO. Over that same
period IPOs sub 75 million have gone from 38 percent to all
IPOs to just 6 percent.

So much larger companies are going public, which
means that every-day investors can't get into those shares,
and miss out on that growth opportunity. And so that's why
the work that you all are doing I think is so important, and
the work that the SEC is doing is so important in this
space. You know, the SEC is in the middle of a year-long
process looking at the proxy rules and the proxy process,
and things like proxy-advisory firms act to the
shareholders, proxy rating, stuff like that is providing a
disincentive to IPO. Not that those shouldn't exist,
obviously they have a valuable role to play, but they take a
lot of time and money to deal with as a small company even
though they don't really have a stake in your business
Similarly, the SEC just had a roundtable on
quarterly reporting, and how the short term look at meeting
a Wall Street target may not align with what your long-term
best interests are as a company
And then, of course, there's the cost of being a
public company. And I know that's what we're all kind of
focused on today. Time and again we have heard from member
companies at NAMM that the cost of being public - going
can be a Wall Street target may not align with what your long-term
IPO, and 404B is obviously a key piece of that

Yes (Unidentified Speaker - I am not to that part
yet)

CHARLES CRAIN: Thank you. And so -- and so
that's why, again, I think it's really exciting that
you all are having this conversation
And so what I wanted to do is talk a little bit
about how manufacturers experience 404B specifically. And
one thing that I think is important to point out, and

Director Hinman did this as well is that this is not a
conversation about 404A. No matter what happens with 404B
under the proposed rule, whatever you all recommend,
whatever the SEC finalizes, manufacturers value and rely on
the 404A internal controls that they are required to do
under Sarbanes Oxley, and -- and those aren't going
anywhere. That's something that's very important for
investors and it is a significant protection for them.
404B, on the other hand, is a different cost
benefit analysis for manufacturers. In the proposal the SEC
cites the direct cost savings, the floor of the direct cost
savings at $110,000 per year, but they acknowledge that
that's a conservative estimate, and that could easily be up
to 200, $250,000 a year just in direct costs. That's the
increased check that you write to the auditor for lack --
for lack of a more sophisticated description. And then they
estimate non - a non direct cost as well of about $100,000
a year. But I spoke to a company the other day where they
were sort of in this SRC bucket, and they have an entire one
person whose only job to do a 404B in house, and their
combined salary benefits is $100,000, and that's just one
person, so I am assuming the rest of their non direct cost
would exceed $100,000, so, you know, when adding those
together it's a quarter of a million dollars, 300, $400,000,
which is significant for our growing manufacturers, and

that's capital that is not going to job growth, economic
expansion, etcetera

Excuse me

When we talk to our companies their main challenge
actually is workforce, and so they might much rather be
spending that capital on up skilling job training. You
know, with unemployment as low as it is they have a hard
time finding workers, so if there was a way to save a little
money on 404B compliance, and divert it to, say
apprenticeships, that's something that would be incredibly
impactful for our companies, and obviously for the broader
economy as we continue to -- to bring folks into the skills
that they need to succeed in the 21st Century economy

There are also significant opportunity costs, so
it's not just the direct dollars and cents. For a small
company management, obviously is dealing with 404B, but, you
know, they are also the senior salesperson, the senior
relationship builder. They are out doing on your road
shows, and so there are only 24 hours in a day, and so if
you are -- you know, every hour you're spending on 404B
you're not out there finding a new client, finding a new
investor. And that's something that our company has raised
with us as well in connection with the direct sort of
dollars and cents cost

And -- and one other thing I want to point out is

that any exemption from 404B, whether under the proposed
rule, under the Jobs Act, under the existing standard at the
$75 million in public float, that's an optional exemption.
So if companies felt that they need to comply with 404B,
they need to have that external attestation in order to give
their investors the comfort they need, or, in fact, if their
investors are saying to them, We're skittish about investing
in you for this specific reason, they are always free to opt
into compliance. The market is actually pretty good at
this. We've seen this with the Jobs Act. Emerging growth
companies are allowed to utilize private company GAP
standards during a transition period rather than public
company GAP standards, and no one is opting into that
because the market has said, We don't -- we don't want you
to do that, we'd rather you have on the public company
standards so we can compare you with your peers.

As you all know, there's also a 404B exemption,
the Jobs Act, and no one is opting out of that. Everyone is
taking advantage of the exemption from the external audit.

So I think the market can dictate this, but
unfortunately the threshold, as it currently stands is so
low that the market is not given the opportunity to make
that decision because these companies aren't qualifying.

So I want to talk about -- I'm going to press this
button and see what happens.
Well -- there we go. Okay. So I want to talk about sort of how we got here, and I know this has been covered by the SEC staff and by Jeff earlier. The current standard, as we know, is at 75 million in public float, which as I've said, in our view and in manufacturer's views is -- is too low, and to the SEC's credit they've proposed to make changes in the space. I just wanted to - to give you all a friendly reminder that this committee or the previous iteration of this committee has recommended changes in this space before, and specifically has recommended taking that $75 million in public float and bumping it up to $250 million. So that's something that you all have done twice in 2013 and 2015.

The government business forum on small business capital formation, which is being held here in Omaha tomorrow has said the same thing every year for the past decade, so there's a pretty clear record that the business community and the investors who participate in these various four think that the 75 is too low, and it needs to be bumped up. And there's pretty clear consensus, in fact, on that $250 million level.

And so when we look at what the SEC has done with this information, there -- there are actually two definitions that play here as -- as Director Hinman laid out, the SRC definition, and non accelerated filer, which has historically been identical. And then you see here when they made the SRC change last year, they certainly took their recommendations from these -- these two forums, the Advisory Committee and the Government forum, and adopted them sort of as recommended with obviously their own robust analysis, but the result is that the -- what was recommended has now been finalized as the new SRC universe.

On non accelerated filer, though, they only kept the revenue prong of the new SRC definition, and not the public foot prong. So there's this universe of companies between 75 and 250 who are deemed sufficiently small to be an SRC, but not sufficiently small to be a non accelerated filer. And relevant to the conversation around 404B obviously they are not exempt from 404B if the proposal were to be adopted as proposed.

And so what we did is we pulled some data on these companies in the manufacturing industry. So we looked at companies above 75 million in public float who are newly SRCS under the 2018 reforms. So we didn't look at anybody below 75 and float because they've always been exempt, they're always going to be exempt, they are sort of not -- not relevant to this conversation. Certainly small companies are glad they are exempt, not really up for debate here, but we looked at these companies that either meet the revenue prong of the new SRC definition or the public float prong of the new SRC definition.

And so if you look at the left side of the slide here you see the low revenue manufacturing SRCS. Again, these are the ones that would be considered non accelerated filers under the proposed rules. You see they obviously have very low revenue, average market value. The -- the average market value for this whole sample is 180, so they are pretty similar to the universe, and you can't see my data labels on this presentation, but I will tell you what they are. That what we did is we broke out by sub industry, so this is all manufacturing, but the -- the darker orange, if you can -- if you're not colorblind, you can see the darker orange are bio pharmaceutical manufacturers, so they are a very important part of the manufacturing industry, obviously. And as has been noted a couple of times, they very specifically benefit from the left side of this slide, which is the proposed change to the non accelerated filer definition that would allow them to newly qualify.

What you see on the right side of the slide, though, is that everybody else within the manufacturing industry is largely left out, so the right side -- those -- those percentages it's like 91 percent and 9 percent if I remember my numbers correctly. So of these companies who now on the right side would not qualify for the new 404B exemption, 91 percent are everybody else, so the proposal very much works for bio pharma manufacturers. It very much doesn't work for every other sub industry within the manufacturing industry. But if you look at the sort of size metrics here on the slide, they obviously do have revenue because they failed the revenue test on the left side of the page, but it's not that high of revenue, the $100 million up to -- is the proposal. 228 is not that far, and in our view they are still substantially similar in terms of what they look like to an investor, and the market value is actually less, as you can see here than the market value from those who would be exempt.

So from a -- from a policy perspective as this committee considers what -- what to recommend, and as the SEC considers what -- how to finalize the proposal, you know, there's a specific policy choice to be made around who qualifies and who doesn't. And in our view you shouldn't leave out the rest of these manufacturers. They are creating jobs across the country, and they are still small businesses. I mean, that's the key here, that the goal is to identify who should be considered a sufficiently small business to qualify for this exemption.

And I -- and I would note that the charter of this advisory committee charges you with looking out for the needs of any company with a market capital of $250,000
Jeffrey Solomon: Thanks, Charles. Appreciate your perspective. David?

David Maley: Hello. Thank you, Committee, for asking me to speak on the proposed amendments to the accelerated markets, accelerated filer definitions.

As Jeff said, it really is an honor and a privilege to participate in this process, so thank you again.

You're not going to hear me advocate strongly in either direction on these proposals. Rather what I am going to try to do is share my insights as an investor who is focused on the small end of the US equity markets, and hopefully that will help shed some light on the practical implications of these definitions, and -- and obviously the proposed changes.

I have been in the investment business for 35 years now. I started out in a cell site at Goldman Sachs in Chicago. I spent eight years as an institutional salesperson, and there I discovered that I loved the markets, but I want to do what my clients did. I want to be a stock picker, I wanted to be an investor. So I am not being a portfolio manager for 27 years, and the last 20 I have been focused on long-term value investments in micro issuers, and I think there's a real opportunity for it's complicated for investors and it's complicated for but I have this revenue, and it's -- it's complicated, and fits in which definition and I'm small and then I'm over 75, this every day, I think it's a significant barrier for small obviously, but given the confusion amongst the folks who do this every day, I think it's a significant barrier for small companies to overcome when they are trying to figure out who fits in which definition and I'm small and then I'm over 75, but I have this revenue, and it's -- it's complicated, and it's complicated for investors and it's complicated for issuers, and I think there's a real opportunity for technically the case Appreciate the recommendation obviously, but given the confusion amongst the folks who do this every day, I think it's a significant barrier for small companies to overcome when they are trying to figure out who fits in which definition and I'm small and then I'm over 75, but I have this revenue, and it's -- it's complicated, and it's complicated for investors and it's complicated for issuers, and I think there's a real opportunity for

Regulatory alignment here in addition to the fact that this is -- this is costly and -- and burdensome for small businesses.

Jeffrey Solomon: Thanks, Charles. Appreciate your perspective. David?

David Maley: Hello. Thank you, Committee, for asking me to speak on the proposed amendments to the accelerated markets, accelerated filer definitions.

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Cap and small cap companies. I managed my own firm for about ten years before I joined Ariel Investments in early 2009, and I brought my portfolio strategy to -- to the firm.

I am based in Chicago. Ariel manages about 13 billion along with the equities in three broad strategies. The firm was founded in 1983 by John Rogers as a small cap value manager, and John has always used a Warren Buffett-like approach, buying quality companies with solid growth prospects at prices below their long term intrinsic value. He's still our chief investment officer and our co-CEO, and he built the firm over the years from a small cap up into Smitt, and even some large cap investing.

And then when I joined in 2009, I brought a second strategy, and we called that deep value. We're foc -- I am focused on a micro cap in the very small end of small cap using more of a Graham and Dodd value approach. That is I am more of an asset-based investor looking for mispricings in a, we think, much less efficient part of the market.

And then our third leg of the stool was added in 2011 in the form of a global international team, which is based in New York.

Now, the one thing that we all have in common at Ariel is we're all long-term value investors. Our motto is slow and steady wins the race. Our logo is a turtle. Jeff has been in our office. He's seen there's probably thousands of turtles in the office. We are really long term, patient investors, and we all run pretty concentrated high conviction portfolios, and all of us care deeply about the quality of the financial reporting of our companies.

And our clients generally care as well. About a third of our assets are mutual funds, but the rest is in separately managed accounts for pretty sophisticated large institutional investors, private and public pension plans, endowments, foundations, large family offices. And our management agreements with those clients usually authorize us to manage their assets in accordance with one of our strategies, but they'll also from time to time impose restrictions, which are usually designed to control risk as they see it. And among those restrictions are restrictions on the type of securities including different classifications of equities that can be purchased and/or held in the portfolios.

Now, I manage the only portfolios at Ariel, as you can imagine, that are affected by the difference between non accelerated, accelerated, large accelerated filers, and therefore, which could be impacted by the proposed amendments.

To date, we've not made any formal distinctions in our process between non accelerated filers, accelerated filers, large accelerated filers, and nor ever done so with
regard to smaller reporting companies. Where we have made a distinction is between listed and non listed securities. We don't buy pink sheet stocks, we don't buy OTC bulletin board stocks. And, in fact, some of our clients have imposed restrictions on those, but even absent a client restriction, since we believe financial reporting is so important and it's likely to be mediocre, even worse in those stocks, we have no interest in that part of the market.

And so as I said, we do care deeply about the quality of the company's financial statements, and there's this perception that micro cap means risky. And we want to take the risk of fraudulent reporting off the table right away. So, again, all of our companies, you know, file 10Ks, 10Qs, proxies, they are all listed, and I don't believe that the portfolios that I run at the very small end of the market have a materially or greater risk of fraudulent reporting than any other of the portfolios at Ariel, and so that's very important to me and to my clients.

And so as I looked at these specific amendments -- proposed amendments, I ask myself basically three questions, one, obvious simple question: Do we own any non accelerated filers? And the answer is, yes. I'll come back and give a little detail. Do we value the ICFR Auditor Attestation? Yes, and, again, I'll elaborate on that.

And finally, if a proposal is adopted and the companies with revenue under 100 million no longer need the ICFR auditor attestation, what impact is that going to have on our process, and not by extension on my deep-valued portfolios, and that's an open question. I'll come back and touch on that.

So go back to our Question 1. I run two different deep-value strategies, as Jeff mentioned earlier, a micro cap portfolio, and what we call small cap deep value. And the only difference in how those are run is the upper limits of what we can buy in terms of market cap. So for micro cap we can go 500 million and under initial purchase, small cap we value 2 billion and under, but our averages are much smaller. The micro cap's dollar-weighted average is 140 million, and the small cap deep value is 240 million.

So, again, we really operate in a very small end of the market, really the -- the area that this committee is concerned with.

There are about 30 names that are in common to the two portfolios, and those generally have capitalizations I'd say in the range of 50 million to 500 million. And there's a handful of really small names in micro cap, and a handful of larger names in the small cap deep value. So there's 43 total companies that I own, and six of those are non accelerated filers.

Now, of those six, five I have owned for at least six years, and there's even two that I owned before I came to Ariel more than ten years ago. So, again, you can see the long-term approach. And with such a long history with those companies, I'm very confident in the management teams, I am very confident in the quality of their financials.

So the one non accelerated filer that doesn't fit that description is my second smallest position, and it may or may not be coincident, but it's probably of all the names I own I have the least confidence in including the quality of its financials.

Now, Question 2, do we value the IS -- ICFR attestation, you probably can tell the answer is yes. Now, as a deep value investor, I am looking for mispricings of assets and/or ongoing businesses. So I like growth, but I don't want to pay for it. I view growth. It's very small companies, it's unpredictable, and therefore I'm really not willing to pay a lot for it.

So on Page 26 of the proposal there's a passage that refers to biotech and similar small, high growth low revenue companies. "We believe these and other low revenue issuers would potentially benefit from the cost savings associated with non accelerated filer status, and could redirect those savings into growing their businesses without significantly affecting the ability of investors to make informed decision based on the financial reporting of those issuers."

I don't disagree with that at all when it comes to a newly public biotech, or one in its first couple years, but I don't buy that type of company. That's not relevant, to at least what I do. Instead, I tend to invest in more seasoned companies that have become orphaned by the market. My bread and butter is under followed and overlooked in special situations. And the passage on 25 from the proposals is more relevant, at least to me. "We continually believe that ICFR auditing attestation requirement incrementally can contribute to the reliability of financial disclosures, particularly for issues that have more complex financial reporting requirement and processes."

So the idea of the market value of a company is more driven by its future prospects than by the current periods financial statements is only partly true in my world. If I can buy a dollar's worth of assets for 50 cents, I am thrilled, but I need to be sure that those assets are truly worth a dollar.

So on to Question 3, which is probably the most important. As you can see, we don't typically invest in the companies that this proposal is designed to benefit, so how will it impact us if it's a doctor?

Of the stocks that I own, which are now accelerated filers, an additional 15 have revenues under
100 million, and therefore could become non-accelerated
filers, so therefore roughly half of my current holdings
would note—would not need to obtain an ICFR attestation
from an independent outside auditor.

Now, each of those companies would clearly obtain
some cost savings, but there is not one company where I
believe the investment thesis would materially improve by
eliminating that cost, whether it's 110, whether it's even
up to the 3 or 400,000. Charles said, Yes, those are
meaningfully, but I don't think it changes the investment
case. But there are quite a few where the attestation
provides additional comfort to me in the quality of the
financials. These are small public companies. They are
often in industries that are out of favor. And therefore,
they are probably on average more likely to have less depth
in their management team, weaker boards, and therefore be
more susceptible to—don't want to say fraud, but less
— you know, less robust financial reporting.

So absent this attestation requirement, we would
actually, I am sure, take a formal re-examination of our
process and determine the need, if there is any, for a
formal delineation between non-accelerated filers and
accelerated filers. Again, we haven't done that in the
past, but I think we would at least need to examine it.

The other potential reaction—issue is the

reaction of institutional clients. Upon an announcement of
this proposal being adopted, it's not out of the realm of
possibility that some plans might restrict ownership to
accelerated filers. But even absent formal restrictions
there is some risk of the pool of non-accelerated filers now
being seen as a particularly risky subset of the micro cap
world.

So in summary, I see clear—clear pros and cons
of the proposed amendments. There's a group of low revenue,
high potential growth companies that would clearly benefit,
and that might help invigorate the IPO market. In fact, it
probably would. It would spur interest in micro caps as an
asset class, that's all good, but there's no free lunch.

Confidence financial reporting is crucial to properly
functioning markets, and it might take more work to make
sure that we keep that confidence. Thank you.

JEFFREY SOLOMON: Great. Thanks, David.

I think we're going to do this. Hopefully—we
haven't had a big talk, so hopefully everything works here.

TERRY McNEW: This is Terry McNew, can you hear?

JEFFREY SOLOMON: I think we can hear you. Go
ahead.

TERRY McNEW: Okay. Great. Thanks. As you guys
know, I—I run a small cap public company. I have
been working with the National Association of
mid 2021

So our adult -- I took our audits public in 2014, initially invested in the company in 2007 on -- as an emerging growth company, which enabled us to access the kind of capital markets that we need to ensure our growth, and we're fortunate to have the Jobs Act that allowed us to do that.

Next slide, please.

The Jobs Act of 2012 has been a success for biotech. The IPO on ramp, or the five-year exemption for emerging growth companies from auditor attestation, internal controls, has been important. Jobs Act is almost 90 percent of all IPOs are emerging growth companies, and roughly 40 percent of those are biotech.

We have 200,000 -- 200 percent growth and employment biotech since the Job Act was enacted.

A couple of key numbers under the Jobs Act is we've had 332 IPOs, 91 preclinical Phase 1 IPOs, 29 newly approved novel drugs, and almost $30 billion raised at IPO for those companies. And without the Jobs Act Ardelyx would not have been able to access the public markets to finance the work that we've been doing over these last five years.

So the IPO -- the next slide, please.

So most biotechs go public early in their 10 to 15-year development time lines because to access the kind of capital that we need for our clinical work is not really doable in the context or private financing. And the five year 404 exemption typically comes well before any of us are generating revenue. Ardelyx is a good example of this.

Compliance with 404B means that biotechs must divert capital from research in the middle of the drug development process, and a growing number of companies will have to divert money to compliance after their status ends if the rule isn't finalized.

So what is -- next slide, please.

So what is 404 compliance costs biotech on an average of $800,000 per year? For Ardelyx as we are aging out, our consultants, we spend $450,000 already. Additional auditor fees from Ernst & Young is about $600,000, you have eight full-time employees working on the project. What the consultants do do 100 percent checks of the controls to make sure that we're following what we say we're doing. Ernst & Young then checks 100% of those controls to make sure that we're following what we say we're doing as well.

And all this is happening in a span of the last couple of months to be ready.

The value is we're really already doing most everything, and now the only thing that we need to do is further prove it with those costs is would it have been better to war -- to direct that towards our clinical trials where you can imagine eight researchers could have been covered with that at roughly $100,000 a year, or an additional eight to sixteen patients could be enrolled in our clinical studies, which range from $50,000 to $100,000 per patient in most clinical trials. Most of our investors in biotech are focused on the science behind the company, and have never demanded, and can't imagine since we have 404A, would demand 404B.

Next slide, please.

So expansion of 404B, relief for companies until they exceed 700 million in public float, or at least what we responded to was or 100 million in revenue is a welcome step forward to making our public capital markets more accessible.

Bio and member companies, such as Ardelyx are pleased that the SEC recognized that 404B should be more appropriately tailored to the actual risks. While we fully support the proposed rule because of the expanded 404B relief, it will provide for many more small biotechs.

I also want you to know that there's still some biotechs that do not pose the risks for which 404B was designed, but may not be eligible for the proposed exemption because they not do -- do not meet both the public float test and the revenue test.

It's really not uncommon for biotech companies.
that are pre revenue and have simple financial structures with public float exceeding 700 million. Similarly, there are examples of small biotech companies that exceed $100 million in revenue simply due to partnering revenue that isn't product revenue, and is not necessarily recurring revenue.

So I applaud the SEC for its proposed rule. At a minimum, I urge them to adopt it, or I suggest that you should consider expanding it further and changing the "or" to "and," as there are unintended consequences of using the word "or." But I've been pleased to hear that Mr. Hinman and Chairman Clayton did use "and" in the discussion, so I hope that that thought continues.

I would like to thank the SEC for taking steps to expand the SOX exemption, and committed for its continued attention to issues that impact small public companies, such as companies like Ardelyx entering and staying in the public markets.

Thank you.

JEFFREY SOLOMON: Great. Thanks, Mike, and thank you, all of our speakers. Let's let's open it up for dialogue, or for questions. I think -- you know, I think we've heard there's sort of the biotech/nonbiotech part of this discussion, which is an important one. And also I think we've heard about some unintended consequences, and I would encourage everybody on the committee, or obviously any of the Commissioners, or anybody who wants to speak up and ask questions.

TERRY McNEW: Jeff, this is Terry McNew, can you hear me?

JEFFREY SOLOMON: Yes, we can.

TERRY McNEW: Okay. Sorry, committee members, I'm not able to be there today, but it's actually a bit ironic, I have an audit committee and an outside audit meeting this afternoon and tomorrow, so I was unable to be there.

Related to dis -- earlier discussions on 404B, I work closely, as you know, with the National Association of Manufacturers. I run a consolidation of companies with a 300 to 700 million market cap, and to Bill Hinman's comments about an hour ago, and to Mike's just a moment ago, I actually have a breakdown or our 404B costs. Now, we fall outside of the Jobs Act and emerging growth status in about a little less than 18 months, but our first four years plus of being a public company, annual estimated cost of Sarbanes Oxley is $700,000 a year. Bill was exactly right. There are software costs of just under 100,000. I have an internal Sarbanes Oxley manager. It's about 190,000 in incremental costs from the 404B. We have to get opportunity costs, but a lot of it is just the auditor outside audit costs of nearly 200,000.

After we lose our -- our emerging growth status, year six and thereafter, we estimate that our annual Sarbanes Oxley 404B costs would be just under $1 million, and so as a 600 we have just under a half billion in sales we're able to -- to, you know, compensate for that, but being a public company is expensive. It costs us probably around 4 million in total costs to be public, so I -- I applaud the comments earlier to balance both investor and company business needs. It -- it -- it's very much -- it's necessary, but I, like others, have never had an investor ask me about 404B. We're 404A, of course.

I have already conducted nine non deal road shows and investor conferences in the first six months of this year, and I generally do about 10 to 12 a year, and -- and not once have I had that, so the level today of revenue is 75 million. Assume your 5 percent net income at that level, which is -- is a bit of a stretch, but possible. Assume that's just under 4 million. That -- that equates to about 24 percent of your net income as being consumed just to be 404B compliant. So I would like to respectfully request keep the 700 million market cap requirement, and as -- As Chairman Clayton, Mike just mentioned, put the word "and" in there, but raise the revenue level from 100 to 250 million.

It sounds like a lot, but you're still a small company at that level.

I could literally with 3.5 million, 4 million and additional net income, I could double product development, which would be, you know, wildly important of the company in tune to invest itself.

I just wanted to provide a little bit of actual business perspective and -- and costs and recommend that the committee consider and that the chairman consider raising the revenue cap up to 250 million.

Thank you.

JEFFREY SOLOMON: Thank you, Brian?

BRIAN LEVEY: We're going through 404B right now because we will no longer be an emerging growth company at the end of this year, and we're not going to fit within any of the exemptions being proposed, even at higher levels, but I can just walk folks through sort of our direct incremental costs related to 404B attestation. It's about a million a year incremental. It doesn't even include, you know, the SOX person who is likely to be, you know, 150, 200 at least. It doesn't include others in finance in the non 404B costs, it doesn't include obviously our opportunity costs, but a lot of it is just the auditor incremental costs from the 404B. We have to get...
another smaller audit firm to lead the project, and that's a good amount. The software upgrade for us is about $50,000, and then I think it was mentioned earlier -- I think Charles mentioned that we can no longer take advantage of the -- the private company GAP standards, so their cost to adjusting to the public company GAP standards in my finance team tells me that ASC 842 is just an example. And that's another $80,000 that the auditors will charge just for piece. So it is real. Certainly understand that, you know, there could be highest malfeasance as a result, but I will say that in the post Enron era it's awfully tough for companies like us, public companies to switch auditors. I find the auditors have become extremely thorough. The 404A certification certainly make our CFO and CEO very nervous. We conduct sub certifications across all our functions to make sure that they can sleep more easily at night. And then I think we can't forget just the whistleblower bounties that are out there now that can take care -- at least incentivize reporting of malfeasance too.

So to me I think, you know, very much welcome these proposals even though we can't directly avail ourself of them, but certainly see the advantages out there. And to the extent that, you know, this does become voluntary, it's obviously something that makes sense for audit committees, for companies. And to the extent that a post mortem review is needed to review whether there's increased cash -- cost of capital, to the extent there is more malfeasance, that's probably a decent idea in several years just to see how the proposals are doing, so just some quick observation from my perspective.

JEFFREY SOLOMON: Other questions?

Burt?

ROBERT FOX: Well, I mean, I guess I am curious on some of these items. Like you talked about 800,000. And, Brian, I know you're general counsel and not the finance team, but, you know, it seems like some of that is probably things that would have, should have been done under 404A maybe. I don't know. I mean, I am trying to -- to understand what that difference really is, right?

I mean, Carrie, I think I heard you say that you're spending around 700 right now to comply with 404A, and you'll spend another 300,000 essentially getting it attested to. I think that's what I -- I heard.

And -- and so, I mean, I guess I am -- I am curious, and I like David's take of, you know, as an investor, does that give you pause that, you know, even the non accelerated filers may or may not be actually doing, you know, what they should to even comply with 404A, and I'll also follow that up with a -- you know, in -- in the SEC's comment, or their proposal, I think they state a stat, but -- and Bill or Jennifer, correct me, but I think it's at 40 percent of non accelerated filers on a pad of material weakness, or some sort of control issue reported from 13 to 18, I think I am trying to remember that I don't have it in front of me, but it's something along those lines

UNIDENTIFIED SPEAKER: Those numbers are higher, but --

WILLIAM HINMAN: Yeah, one of the things to bear in mind is that is not the universe that gets relief here

UNIDENTIFIED SPEAKER: Right

WILLIAM HINMAN: It's a different group. It's a bigger group

UNIDENTIFIED SPEAKER: Yeah

WILLIAM HINMAN: But, yeah, in terms of folks that weren't an attestation of the universe that we could look at that the economist -- the economists looked at were below 75 million. I think you have the numbers probably in the ballpark

ROBERT FOX: Yeah

WILLIAM HINMAN: But that's not the group we're looking for

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Robert fox: So, I mean, David, I am curious from an investor standpoint, does -- I mean, what's your reaction to that?

DAVID MALEY: Yeah, I mean, there's -- there's a lot to unpack here. I -- you know, the -- the cost of just 404A are very high. And, in fact, in talking to a lot of the CEOs and CFOs, the cost of just being public at the smaller are very big, and that's no secret to anyone. And that extra cost to be -- you know, I am sure it's going to be different for different companies. What it does for us is it's just that extra level of knowing that there's another level.

Now, again, we own some stocks that don't have that right now, and we're very comfortable with them, and one of those is a case where the CEO is trying to figure out ways because he has different subsidiaries and he has to just to get the 404A is extremely costly for such a small company, and one of the answers may be no longer be public. And so, you know, we're sort of in that -- in that world where we want there to be a thriving public market for companies, obviously that's what I look for, but oftentimes the best realization of value for these companies is to no longer go public, and so have that turnover into a way that -- you know, that they be comfortable.
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<td>So it's -- again, it's an extra comfort level, and</td>
<td>accelerated filers  All of those we rely on controls</td>
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<td>if you add this to the mix, I think -- I think we're going</td>
<td>during the audit process unless there is a material</td>
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<td>to at least have to have a formal review that says, How do</td>
<td>weakness, or some other issue actually with their</td>
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<td>we treat these because there's a big part of our world that</td>
<td>controls  You know, and so it is a true -- I mean,</td>
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<td>no longer has this. I don't know that it -- that it means</td>
<td>the days of -- you know, the first day of 404 when we</td>
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<td>that there is anything that we own now that we wouldn't</td>
<td>literally had two different teams, one doing controls</td>
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<td>continue it on. I doubt if there is, but I think we'd have</td>
<td>and one doing substantive audit have gone away  I</td>
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<td>to do more diving, and I think others like us would, so it's</td>
<td>mean, we -- they are all integrated audits now  So</td>
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<td>not an easy answer, but there -- you know, there's like --</td>
<td>it's not a one for one  There clearly is additional</td>
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<td>so there's a lot of cost there even without the B.</td>
<td>work of -- of us auditing and documenting the control</td>
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<td>ROBERT FOX: I mean, because my perspective from</td>
<td>work if that's your question</td>
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<td>what we see in practice, and, again, you know, from my</td>
<td>You have the non accelerated filers  We -- to</td>
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<td>firm we audit just under 300 or so issuers. The vast</td>
<td>Bill's point, we still have a requirement to understand and</td>
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<td>majority of them have a market cap under, you know, a</td>
<td>evaluate controls, which is where a lot of these material</td>
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<td>billion dollars. We have some that are over</td>
<td>weakness things are coming from  But normally if an error</td>
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<td>two-thirds of those 300 or so are accelerated filers</td>
<td>is not found, there -- you know, that -- that's kind of more</td>
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<td>right now, but on that small end of that space, I</td>
<td>where the control weakness comes in through the substantive</td>
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<td>mean, you definitely see that, you know, there's less</td>
<td>audit we actually find something, and in which case is it's</td>
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<td>sophisticated finance teams on average, there's less</td>
<td>kind of that early preventive wire of the control testing,</td>
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<td>sophisticated systems. There are more errors in the</td>
<td>you know, would have had -- you know, it -- ideally you</td>
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<td>financial statement that we find in that space, and --</td>
<td>would detect it early saying, Hey, they could have been in</td>
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<td>and, you know, a lot of these $200 million revenue</td>
<td>error because the controls aren't working  It actually</td>
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<td>companies do have multiple entities, are operating</td>
<td>waits until the error is actually detected, and then that's</td>
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<td>internationally, they -- there's not necessarily -- I</td>
<td>kind of when it's being reported</td>
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<td>don't think you can say there's a direct correlation</td>
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<td>CHAIRMAN JAY CLAYTON: Jeff, would it be okay if</td>
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<td>between simply, say, $250 million of revenue and low</td>
<td>I made observation then sought input?</td>
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<td>complexity. There's a lot of companies in that space</td>
<td>JEFFREY SOLOMON: Absolutely</td>
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<td>that have a lot of complexity to them, so --</td>
<td>CHAIRMAN JAY CLAYTON: A couple things  I want</td>
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<td>JEFFREY SOLOMON: So just out of curiosity, I</td>
<td>to say that high quality financial statements,</td>
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<td>mean, one of the things that we've heard is that, you</td>
<td>including a high-quality audit is the bedrock of our</td>
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<td>know, without auditor attestation, that's really what</td>
<td>capital market system, and I think the approach in the</td>
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<td>we're talking about here for the most part, because</td>
<td>US has actually lifted the rest of the world  The</td>
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<td>404A is not really on the table.</td>
<td>last things that I would want to do is do something to</td>
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<td>ROBERT FOX: Yeah.</td>
<td>harm that, so that's sort of the baseline  But the --</td>
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<td>JEFFREY SOLOMON: So there will be a lot of work</td>
<td>I think with -- you know well over a decade of</td>
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<td>that has to get done anyway. How much of -- of those</td>
<td>experience with 404B and at least, you know, half a</td>
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<td>-- how much of those companies that you do the work</td>
<td>decade of experience with the Jobs Act relief from</td>
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<td>for would fall into a control audit function as</td>
<td>404B for certain companies, the market is telling us</td>
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<td>opposed to a sub -- or a substantive audit as opposed</td>
<td>something  Now, you don't -- you don't listen to</td>
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<td>to a control audit? I think that's actually something</td>
<td>everything the market tells you, but it is telling us</td>
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<td>that, you know, we might consider because if companies</td>
<td>something  I -- I -- I look at the private space</td>
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<td>stopped doing, you know, auditor attestations, there</td>
<td>Let's just look at the private space  In the private</td>
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<td>is work that gets done by the auditors. Then all of a</td>
<td>space you have private equity firms, you generally</td>
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<td>sudden, you know -- or if they do them every other</td>
<td>have lenders, you also have bond holders  These are</td>
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<td>year or every third year, how much of the -- of your</td>
<td>people who care a lot about their money  I'm</td>
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<td>population do you think falls then out of the control</td>
<td>clamoring for 404B attestation  In fact, no one has</td>
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<td>audit and into the substantive audit, which is</td>
<td>ever come to me and said, Will you please add a 404B</td>
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<td>expensive?</td>
<td>attestation to a company that uses the high-yield</td>
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<td>ROBERT FOX: Again, we have slightly under 300 or</td>
<td>market for over, you know, a billion dollars  That's</td>
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<td>so issuer clients, about 2/3rds of them I think are</td>
<td>not even -- I don't think it's ever crossed their</td>
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You know, and then you look at the US/non US market, and I don't know many portfolio managers. David, I would be interested. You know, it's a non US small caps, mid caps, no 404B attestation, you know, in some cases, you know, whatever.

DAVID MALEY: We don't do small cap foreign because it's — that is the Wild West, I think.

CHAIRMAN JAY CLAYTON: Yeah.

DAVID MALEY: There's probably opportunity, but

CHAIRMAN JAY CLAYTON: So I think I'd like to know, you know, what — are there people that make a difference, doesn't make a difference? It seems valuation aren't that much different. It's converged. Maybe there is a Wild West premium. I don't know. I am just asking.

DAVID MALEY: Maybe. Yeah, I mean, I don't know how those markets work.

CHAIRMAN JAY CLAYTON: And then, you know, sort of — we now have this experience with the Jobs Act, companies rolling off. I don't know of anybody that is, like, rubbing their hands saying, I can't wait until they get their 404B attestation so I can invest. So those are the kinds of things that I am seeing that that make me think. Hey, it's time to also recognize that Congress has told us that with Sarbanes Oxley 404B makes sense, that with the Jobs Act it doesn't make sense for everybody. You know, are we calibrating this correctly, so those are sort of just my perspectives on this.

CHARLES CRAIN: And just from the — from the company perspective, having talked to emerging growth companies, to your point, Chairman, if the investors aren't rubbing their hands waiting for your six to — to get their 404B audit, the companies are very worried about rolling off, so it's sort of — the — on the cost side we hear from companies all the time sort of it's a counting down time clock from, okay, this has been a really great cost saver, but I know in 18 months and 12 months and six months that I am going to be next up on the 404B cost trade, so —

JEFFREY SOLOMON: Other comments?

MIKE RAAB: Yeah, to follow up on what Charles just said is we're a perfect example of that at Ardelyx. We are aging out, and, you know, our cost of capital, we're a micro cap 145, $150 million market cap where that million dollars that I am spending, or just spent over the last six months is extraordinarily expensive capital.

...
at least at the outset, to be honest, that we had a third-party auditing firm. I was a little bit stressed that it took them so long to get it done. We were pushing them significantly against a deadline that was, you know, an SEC deadline frankly, so it was actually one of the more stressful things I remember about getting our deal done. And then I just questioned whether or not it was something that we needed to do every year. We're -- you know, and I think for us again, not similar to what you're talking about, Brian, it's cost us about $4 million a year to be a public company, not all that is the attestation, right? So being public is -- is -- is going to mean that you have more requirements. But I just ask the question, you know, do we need to have the attestation every year, or is it just -- is it -- it is too often. And I'll tell you my -- the response I got from our internal team is if we don't have the attestation, then we're probably going to end up paying for it in the form of a -- of an audit anyway because during the int -- because the teams are integrated, so much of the work that we're doing is -- what we would get we'd have to pay for in the audit function anyway, it wouldn't be so broken out.

So I -- I also will say we are not anywhere -- we're -- from a revenue standpoint we don't meet any of the tests, so none of this applies to Kalin. But when we were a sub $250 million company, it was a much more meaningful number for us than it is now that we're north of the $900 billion a year revenue company. And so like a lot of other things, scale does matter, and -- and so as -- as, you know -- you know, as you think about -- as we think about the marginal costs, I think if you look at who we're trying to include in this group, it's a very significant cost for companies that are under $250 million. It's a very, very significant cost, and, again, as they grow, it's a lot less expensive, so I -- and I don't know that -- I can't draw any specific conclusions from our own experience other than to say, you know, at the outset I was very comfortable with it, but I'm not sure we had to do it all along the way, and I would certainly say for the companies that -- that fall under this accelerated filer, you know, status -- or non accelerated filer status, it's -- it's probably going to be a heck of a lot more meaningful, so --

**DAVID MALEY:** Jeff, maybe if I could add to that. If you think about, you know, the biotech companies, if that's what I invested in, I would be behind -- very much behind because it makes a lot of sense. You've got, as you said, simple financial statements, etcetera. If you go back to when we got invested -- involved in Kalin's stock two or three years after you've done a reverse merger, you're a pretty complex business. There's a lot of confidence that we have that, you know, this group of people who seem to have talent and an idea had merged into this shell that was kind of a mess, and that you had all of the auditing and attestation so everything was a benefit to know that now we could start looking at the nature of the business. Again, if you go to biotech, it's all about the signs and symbols. So I think that's the trade off you have here is how do you make it work for everyone, but make sure that you still have it.

**CHARLES CRAIN:** It seems to me if -- if other investors have that experience where they are -- if -- if those controls -- or excuse me, if that attestation had been lacking, that either there would be a lower valuation or a willingness to invest generally, then companies will do the attestation, and so there -- there was a fair amount of, I think -- you know, let the market play it out here.

**UNIDENTIFIED SPEAKER:** That's a really good point.

**ROBERT FOX:** However, I think to Chairman Clayton's point earlier, if we look overseas, look at the UK right now, I mean, I'd argue that they are having quite a bit of issues, and I think it's unfortunate that a lot of the noise over 404B has potentially poisoned the well because I think we actually have a very successful regulatory model that has proved itself that -- that I think they could adopt. Now I think they are looking at other ways to go down the path, but, you know, we're not seeing the types of issues that we had here in the US. I mean, I was an employee of Arthur Andersen and rode the ship down, and -- you know, and -- and I am seeing across the seas a lot of that history repeating itself right now, right, that doesn't have the same model. And so I totally get the biotech thing, I totally get, you know, some of this stuff. I am not trying to argue that 404B should apply to everyone, but it does seem to me that when I start looking at companies in the $250 million market cap space -- when you start going up to there and you start saying revenue should be 250 or more, you are starting to get a lot of companies that have complexity that it seems to that the -- the incremental benefit to investors -- I'm not sure we're capturing that just in the incremental piece here, so --

**JEFFREY SOLOMON:** Charles, you know, you showed us a median number in your -- in your slides. I would be curious to know, you know, more -- when you crawl underneath that number and you actually look at the number of companies if you were to -- if we were to --
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<td>to incorporate or average or something like that? CHARLES CRAIN: Yeah, so I know - I know congress has looked at that for 404B specifically for companies that are rolling off of AGC status with biotechs specifically in mind, and there's a bill that hasn't become law yet, it exists and it's exactly that, it's a three-year rolling average to -- to kind of call out some of those milestone payments when you're at 000, a hundred million 0000</td>
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<td>BRIAN LEVEY: Yeah, because it's my understanding the biggest costs for 404B compliance is in your one that once you get the SOX environment there, it's lower after that, so to have to comply in your one, and then not to have to comply with -- not to -- for perception purposes not need to comply, it just seems a little anomalous. JEFFREY SOLOMON: All right. Other -- other questions? Because we want to make sure that we leave time to formulate our recommendations, to the extent that we have them.</td>
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<td>committee. It sounds to me like some people were suggesting going farther, and whether that should be -- should all reporting companies, smaller reporting companies, be non accelerated filers, should we increase the amount of revenues? Instead of being 100 million, should it be something higher, 250 million? Should we look at three-year rolling average revenues? So if I am correct in summarizing some of the committee members thoughts on that, can I get some feedback in terms of those three different suggestions that I just stated? JEFFREY SOLOMON: So maybe obviously on one of these. So is there anybody on the committee who doesn't agree with the proposal as it's -- as it's written? And that just -- and then we've got to, I think, probably do some amendments to it. So if there's anybody that's not -- not in favor of the proposal, like we should hear that now, or otherwise I think you can say that at a minimum the proposal as written is something that we could recommend, but then I think we can go through some of the other things maybe along the way and see how the rest of the -- CARLA GARRET: I agree. Is there anybody that's not in favor of the proposal that the Commission has released?</td>
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TERRY MCNEW: And that's the 100 million revenue hurdle?

JEFFREY SOLOMON: That's --

CARLA GARRET: Yes, so it would add to the definition of a -- well, a non accelerated filer would be somebody that has less than 100 - 100 million in revenue.

TERRY MCNEW: I -- I would support it if that's the committee's decision. I still highly recommend 250, and I'll just make this closing comment, keep in mind the market is telling us something. The number of public companies has dropped by 50 percent in the last approximately 20 years. The -- the money that's out there in private equity is -- is huge and it is growing. If there was an overwhelming with infidelity in financials, the market would not be heading in that direction. I know there's risk, but it's expensive, and I get questioned often by investors, why don't you consider going private. That's not my call, but the math suggests that I could roll several million dollars to the bottom line, so I -- I understand there's -- there's complexity even up to 250 million in businesses, but let's try to understand, you know, and capture -- reduce the complexity if -- if 250 million doesn't statistically raise the risk to investors outside biotech and -- but for everyone, I would -- I would like to see an increase to 250. If the committee feels 100 is fine, you know, I'll certainly support that, but -- but I think $100 million revenue company it's eating up their bottom line, and -- and you can do it. Like Charles said, you can still volunteer to do it, your 404A. You know, if you get good business ethics, you're going to make sure your books are good. So I just don't want to make -- I just want to make sure that we're not trying to regulate this to the 05 offender, does that make sense?

CARLA GARRET: Yes.

TERRY MCNEW: Thank you.

CARLA GARRET: Yes, and I think supports what Jeff was saying that you're -- that you're in support of the rules as currently proposed, and so now you want to expand on that and if you would like to add to the Rule B suggestion.

JASON SEATS: One thing I wasn't sure if it was -- we kind of joked about, but is the new addition of 100 million?

WILLIAM HINMAN: Less than 100 million in revenue and less than --


CHARLES CRAIN: But then there's also an "or" factor because you can also qualify, or you have less than 75 in public float. So -- so there's an "or" and then within one half of the "or" there's an "and".

JASON SEATS: Got it. I couldn't tell if --

CHARLES CRAIN: It's confusing.

JASON SEATS: -- it was clear to everyone else, it wasn't clear to me.

CHAIRMAN JAY CLAYTON: I didn't do very well on the LSAT. This is why.

CARLA GARRET: It's confusing. I am a securities lawyer, and I have charts here, and --

JEFFREY SOLOMON: Well, see, yeah, we also -- we also put charts together.

CARLA GARRET: Right. And --

CHARLES CRAIN: And this goes to the complexity point, that if we all have charts and this is our job to do it, it's --

CARLA GARRET: Right.

CHARLES CRAIN: -- it's hard as a small company to figure it out.

CARLA GARRET: Well, and the other thing we might think about is, I mean, last year in 2018 you guys changed the definition of what a smaller reporting company was, and you decided that those companies were entitled to scaled disclosure, and -- but -- but not it does -- and scale -- smaller reporting companies used to be non accelerated filers, and -- and now those two definitions are -- are no longer the same, and that's what is con -- I think creating a lot of confusion.

So one of the suggestions for this committee -- I am not -- is do we actually say that all smaller reporting companies who are -- benefit from the scaled disclosure requirements should be non accelerated filers, and therefore rid of a lot of this complexity.

WILLIAM HINMAN: Right. That is -- that is the second part of the proposal that we actually put forward, right?

CARLA GARRET: Yes.

WILLIAM HINMAN: We did the one we just discussed under 100 million of revenue and under 700 market cap. And then we asked the question, Should the two definitions be the same? You get the exemption if you're an SRC for any test. The second part of that would be any company with less than 250 million in market cap would also -- would be a smaller reporting company, and therefore also exempt, so that's the other piece, which if the committee wants to, they can
say they would favor that or don't favor that second
part of the proposal we put out.

CARLA GARRET: Right.

WILLIAM HINMAN: The question.

CARLA GARRET: Do members of the committee have
thoughts on that?

SARA HANKS: The fewer chance the better.

CARLA GARRET: Excuse me?

SARA HANKS: The fewer chance the better. I
mean, make it easy for companies to understand what
they are supposed to be doing, so, yes.

Second part also approve.

CARLA GARRET: Okay. So if we have -- Jeff, what
do you think?

JEFFREY SOLOMON: So I -- listen, I think scales
disclosure is -- I mean, I have been a big proponent
of scale disclosure for a long time, and I feel like
-- you know, if -- if -- if we're having an honest
conversation, companies of $250 million in market
capital have a difficult time finding investors, and
it's really expensive for them to be that. I am in
favor of scale disclosure for public close of less
than $250 million. I am -- I think the market will
pretty quickly figure out who -- since they are all
complying with 404A anyway, and they should have
complying with 404A anyway, and they should have

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internal controls, the -- if they can't convince
shareholders like David, that they should be
investors, then they need to do things to simplify
their business models and they need to be able to
engage with shareholders more directly.

I think where I end up coming out here is I am
going to do the work anyhow, and I am going to engage with
shareholders if I want to actually increase my -- my market
capitalization. I don't know that we need to have an
external third party accredit -- accreditation to basically
give me that Good Housekeeping seal of approval. It's going
to take time, it may take me longer, but over time it's
going to save me money, and it's going to save me
infrastructure costs probably along the way, and so I am --
I am more in favor of taking it -- making SRCs and non
accredited the same definition. I just think it's an easier
thing to do. That's where I am.

CARLA GARRET: And I would say I support that
too. I -- I was actually general counsel of a public
company when Sarbanes Oxley came into effect, and at
that point in time there were not differences between
large accelerated filers, accelerated filers,
everybody was subject to emergent growth companies,
everybody was subject to the same.

Over time obviously the SEC has decided that
there's a reason why smaller reporting companies or emerging
growth companies should not necessarily, you know, have the
404B attestation. I didn't have that benefit when I was
putting that together for the first time. As Brian said,
it's a lot of work, so I would also be in -- in favor of --
of having all or -- all -- recommending that all smaller
reporting companies be non accelerated filers, so --

WILLIAM HINMAN: Carla, if I could just add one
thing just so the committee has the benefit of it.

CARLA GARRET: Uh-huh.

WILLIAM HINMAN: The -- the reason we led with
the proposal that didn't make the definitions the
same, but the fine tuning for just around revenue of
100 million was the DEER analysis was more supportive
of that in terms of if you broaden the universe of
folks who won't have to attest, the likelihood of
finding problems in the financials down the road would
be lower if we draw the line the way we did, that that
complexity above 100 million actually had some impact
on the -- the DEER analysis. So that -- that is why
we led with that, but we also ask the -- the 250
general question, should these two things just be the
same.

CARLA GARRET: Okay. Thank you very much.

WILLIAM HINMAN: Just so you have that.

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CARLA GARRET: -- did -- did you say you would not be in favor?

ROBERT FOX: I would not be in favor of a vote.  

CARLA GARRET: Of over 100 million?  

ROBERT FOX: Over 100 million, yeah.  

CARLA GARRET: Okay.  

JASON SEATS: Do you have a candidate methodology for how you would measure the complexity?  

ROBERT FOX: Um, I really don't. I mean, I think that the 100 million I could live with because, I mean, again, I totally get the biotech situation, and -- and some of the emerging IT. I mean, again, I think, you know, I could argue that in some of the situations some financial statements are almost irrelevant, right? I mean, what the investors are buying into is the technology and what's going on with the drug trials and everything else in the future, but I think at the $100 million mark I can -- I can live with it because, again, based on the analysis there's not enough companies that are outside of that space that are going to comply with this that it really lose the needle. I think if you take it up significantly past that, I think you are starting to get into, you know, companies that do have a lot -- a lot more complexity, so -- and I think, you know, it's --

it's -- you've got to keep it simple. I mean, you know, you could get into other factors, but then you get into lots more subjective and judgment and everything else, so --

JASON SEATS: So are you saying you would support it at 100?

ROBERT FOX: I -- I could support -- I mean, I don't love it, but I could support it at 100, yeah.

CARLA GARRET: Okay. So I -- I think I -- I have a recommendation here to see and for us to vote on, so let me know what you guys think about this.  

The Committee (sic) supports the proposal to amend the accelerator filer and large accelerator filer definition such that smaller reporting companies with less than 100 million in revenue shall be non accelerated filers. That being said, we would welcome the Commission to possibly explore higher revenue numbers, and also explore whether all smaller reporting companies should be non accelerated filers, and also explore whether or not you should look at a three-year rolling average of revenue.

UNIDENTIFIED SPEAKER: Well said.

CARLA GARRET: Do -- is that something -- did anybody want to comment on that?

JEFFREY SOLOMON: So I -- I just want to -- I want to say one thing that -- so I think that probably works, because I think there probably needs to be more work done between 100 and 250, and we should probably take a look at what that encompasses in terms of the total population of publicly-traded companies is that it's probably significant enough that we should consider that.

I think, you know, where -- where -- where David and I -- where I can agree with David is I think I spent most of my career prior to being in the seat that I am in investing in small cap companies, and what I would say is I don't think I ever thought twice about whether or not a statement was attested. That's not what we're really talking about here, we're not talking about whether or not they are going to be in compliance with 404A because that's -- that -- I wouldn't invest in a company unless I thought that they were doing the internal work and internal audit, and the boards were doing their job, so that's not really -- to me, if I -- if I sit back and think about it I don't think once I thought about, Hey, did they have their auditor attestation as a determinative factor in whether or not I was investing, and that's all we're really talking about here.

And so -- and I also want to say I think one of the -- and I go back to the original for Sarbanes Oxley, the big offenders that -- that got us to Sarbanes Oxley were not small cap companies, they just weren't. They were big, complex companies like World Com and Adelphia and Enron.

And so I -- again, I was investing in small cap companies at that point in time, and the risks to the small cap companies were far more in the camp of they didn't execute on their business plan in whether or not they had their financial statements attested.

I didn't come across very many frauds at all. They just -- they promised a bunch of stuff, they didn't deliver, they ran out of money, I mean, and there was nothing fraudulent. I took their risk, and so I think the market will ultimately adjust to expecting a higher rate of return, which they are already doing for companies that are less than 250 million in free float, that's already happening. And I just -- I think if we're going to make a recommendation, we should strongly consider looking more aggressively at this because I -- I don't -- maybe pulling a bunch of investors -- I mean, David's point of view, but if -- we should be pulling other institutional investors and people who -- who focus on -- on small cap stocks to get a better sense for whether or not 404B is determinative in whether or not they get engaged with companies. If it is, then I think I feel a little bit different because I don't want to preclude these companies from getting investors, but if it turns out it's not that big of a deal, then, okay,
then why are we getting hung up on whether or not there's an external attestation.

Again, 404A is not on the table here, so I -- I would suggest as part of this actual that we actually encourage the commission to engage with a broad base of institution -- I would say institutional investors -- it's hard to get individual investors, but institutional investors in this space oftentimes represent pension years, and -- and individual shareholders as their ultimate investors. Let's go out to that community and find out whether or not 404B is really, really critical to them making an investment decision, and if it is, then I think we can -- well get our answer. That's what I would encourage the Commission to do.

CARLA GARRET: Okay.

CHARLES CRAIN: One other thing that I might add just for all of you to consider is that this committee has recommended in the past that $250 million public float threshold, and -- and that would now represent alignment with the SRC definition.

And to the extent that it didn't recommend it this time, I wonder if that would read as an affirmative dec -- decision that that was no longer a good idea. We used to think it was, and now we decided that it's not, so just something to sort of consider the objects of what the

recommendation looks like given that this committee is already on the record essentially at 250 and float, and -- and if -- if you are as definitive this time, sort of what does that read as?

CARLA GARRET: Well, thank you. We appreciate that, and we do note that this is a different committee, and --

CHARLES CRAIN: Right.

CARLA GARRET: But -- but thank you very much.

So can we have a vote on the proposal that Jeff and I have recommended? Does anybody need it to be restated?

ROBERT FOX: So is it the one you stated -- or Jeff kind of seemed like he had a different --

JEFFREY SOLOMON: Well, my -- my only -- and I guess what I add -- what I would add to it is I would encourage the Commission to actually go back -- go forth and -- and solicit input from institutional investors around the 250, and let's get some data around that. That would be helpful in terms of knowing whether or not we can extend to -- to 250.

CARLA GARRET: So I think that what Jeff is saying is he's adding an additional subject to. We support the amendment as you've proposed. There are a few things that we think that it would be useful for the Commission to look into, and one of those is what investors of whether -- the importance of the 404B.

So may I have a motion to approve that recommendation? Anyone?

UNIDENTIFIED SPEAKER: So moved.

CARLA GARRET: So moved. A second?

HANK TORBERT: (Indicating.)

CARLA GARRET: Okay. All in favor of our recommendation --

(Several ayes.)

CARLA GARRET: All opposed?

(No response.)

CARLA GARRET: Okay. Based on that, then the recommendation by this Committee has been approved, and thank you very much. It was a quite interesting and spirited discussion on a lot of very interesting topics.

CHAIRMAN JAY CLAYTON: Carla, if I could just jump in, and just --

CARLA GARRET: Yes.

CHAIRMAN JAY CLAYTON: -- say thank you to everybody for sharing their views so candidly, it's -- it really helps us. It really does.

CARLA GARRET: Okay. We have about 25 more minutes until 3:30. A couple things we would like to do between this period of time is, first of all, we would like to find out from members what other pertinent capital formation issues the members have that they would like to discuss at other committee meetings in the future, and also other issues that you would like to make members just aware of in general.

So I'll open the floor right now to people that have other ideas to talk about.

Yes, Jason.

JASON SEATS: I have two.

CARLA GARRET: Okay.

JASON SEATS: And they are related, and they are -- they both relate to the -- the definition of qualifying investments under the venture capital exemption, and for -- just so you understand sort of my context that we operate funds, manage funds using that exemption, and the -- and the value that I perceive I am supposed to be bringing to this group is to help understand how -- you know, the things that we learned sort of boots on the ground, how it -- how it applies to -- to capital formation for -- for new and small business, and so the two specific items are the fund-to-funds restrictions and the secondary investing restriction, and the -- the commonality, and think the
applicability to this -- this group is that expanding
that definition for us from what we see would increase
the flow of capital that makes its way into -- into
investment and small companies in the middle -- middle
America and places like -- like Omaha.
And so for -- and to give you a couple of
anecdotes from our company, which is called Tech Stars, and
so we -- we have offices in -- in twenty dozen cities in the
US, and we have employees who are investors in those markets
who -- who invest our capital from our funds into these
companies, but we also encourage those individuals who
raised outside capital themselves, and so it's a bit of a
capital formation, and we're restricted in our ability to
seed that fund formation because there's a limitation on how
much money we can put into those funds, and we don't think
that we are alone, and we see plenty of other coastal
investors who view small funds in these cities as an
important source of deal float for them, and what to see
those funds and create those funds.
And from our perspective because the end benefit
is the same, investing in a venture-exempt entity,
that should flow through to a funds-to-funds level, and
so that's the first item, and then the second is secondary
investing. We invest very, very early, and -- and an angel
investor or a -- a seed fund that invests before us. Even
after 7, 8, 10 years being invested in a private company
will come to us and ask us for opportunities to get
liquidity on their investment, we would love to buy those
shares. We don't perceive a difference in buying those
shares versus about buying primary issuance, and the benefit
to the end market is that those investors who now have a
track record of putting money to work in these companies
will get profits and returns and -- and put them back to
work in new investments, and so those two -- those two items
are things that we like to get on the consideration set.
CARLA GARRET: Okay. Thank you. I appreciate
that.
Yes.
SAPNA MEHTA: And those are, you know, some of --
a few of my items as well, and, you know, I work at
Revolution, and we have a fund called Rise of the Red
Seed Fund, and we like to deploy money throughout the
country, outside of New York, Silicon Valley and
Boston, and we have seen the impact we can have on --
in other cities and -- and in companies where we kind
of provide catalytic capital once we invest.
Oftentimes the companies are able to close out the
round, and -- but the big hole is our inability to
invest and regional funds, and we see that catalytic
capital, like, really picking up speed and velocity in
deployment of the -- of capital to these companies,
but because coastal investors that we -- we can't tap
that expertise that a lot of these regional funds have
given their geographic proximity to these communities and,
and, you know, really knowing that
network and industry, we just -- we perceive that as a
gap, and we don't -- you know, as Jason was saying, as
long as the underlying fund qualifies under the
venture capital exemption, we don't see why we
shouldn't be able to invest, and we, in fact, explore
this option we wanted to create, have a fund of funds,
but given the nature of so many of our investments and
the fact that we would then have to aggregate all of
our funds to become an RIA.
I mean, some of the funds -- I mean, we have $150
million seed fund, and we are invested in over 130 portfolio
companies, and a lot of these companies have four to six
employees. I mean, there's no way -- I mean our current
standards are providing tax-based accounting because that's
just what we have to do, but, you know, to be an RIA is just
prohibitive for us, so we had to walk that back, and we
decided we -- we could not deploy that strategy, and so --
you know, and again with the secondary, I -- I concur with
Jason. I mean, that's also a pinpoint where we think being
able to free up that capital from either early investors or,
The other thing is liquidity is a big issue for us. If there was a secondary market, I mean, we would gladly take advantage of it, and we would deploy that capital back into the market, so just confirming. Thanks.

CARLA GARRET: Thank you very much.

YOUNGRO LEE: Yeah, this is -- I mean, this is really the first session, but I want to -- when -- when Chairman Clayton spoke it he specifically mentioned two things as how do we get capital in geographies that don't have traditional capital, so that's -- that's the reason why we're in Omaha, and the second is how do we actually give the best boundaries to the national investors, and this is more of an expression, but all of the conversation we had today I feel like we barely touched on the second, if at all, right?

Besides saying we're going to change the definition of credit investors hopefully, but, again, that's focusing on the credit investors, and my sense is it's not going to go down, right? If anything, it's going to be additional, so kind of piecing these together, related to the harmonization, but maybe it's just the focus or principle that we should be thinking about if we really want to accomplish Chairmans Clayton's two goals of bring capital to where capital doesn't exist, No. 1, bring and allow the local basically non accredited investors to invest, what do you need to do? And to me that's really two things is incentives. Make incentives for capital to go into -- to physically go into those companies that are not in the outside -- you know, the coasts. And second is an incentive for intermediaries because that is -- I think Jeff expressed earlier, the traditional intermediaries of investing in banks and outside firms are just not going to deal with this space, so how do you incentivize them or the existing players or new players to service it, and that's kind of obviously what the investment industry and the Crowdfunding proffers are going, but one specific suggestion if a credit investor is the top of the agenda is so many non accredited investors would love to invest, I am sure, with Jason or something, like if these accredited investors are investing alongside Jason's company, he's at Tech Stars, right, why can't non accredited investors just invest alongside them on exactly the same terms, and the reason because of the way the laws are, legally Jason cannot accept that.

So even little things like that in terms of how do you change the definition of credit investors, for example, if somebody just trusts their money with Jason, can they invest? Adding those things would be really helpful in a very specific way to address the concern as well as the allowing more people to invest in these opportunities.

JEFFREY SOLOMON: We face this in our own system highlighted, but we -- we arguably have a lot of sophisticated investors in our company. I mean, we have 1400 people globally, and we work in the business.

And we have co-investment opportunities at the time that come through is -- you know, even if we don't take on an assignment to advise the company on how to raise capital, oftentimes, you know, we may be just casually introducing them to people that we think would be -- would have interest. And then they come back to us and they are like, okay, well, you know, maybe we leave a couple of million dollars for you and your partners or your employees to invest in.

And I think one of the challenges we have is we actually have to go through a roster and put out a questionnaire internally to try and determine in a very benign way who is accredited, who is super accredited, who works in the business, close enough with the business to try to figure out whether or not we can get them in under an exemption, and then we have to try to convince the company that they are not taking any risk in that.

And so I would just say even with a business that I think is arguably filled with sophisticated people who might otherwise qualify, I can't sit here and tell you that we're -- we have a clear path, we're doing the best we can to try and get capital overflow from -- from those folks. That would be really helpful.

CHAIRMAN JAY CLAYTON: Can I -- can I -- can I jump in on this?

JEFFREY SOLOMON: Sure.

CHAIRMAN JAY CLAYTON: And, again, I am going to throw this out as sort of my thinking in this area as we sit here today, and I would love for, you know, others from the SEC to chime in as well. But the accredited investor structure is designed for a distribution model. It's designed to protect people in the case of distributing investment opportunities.

And -- and that's what, you know the person is sourcing the opportunity and the person investing are different. The source gets paid for that transaction, and they are gone.

What you just, Jeff, and I think it was co-investment opportunity, and, you know, where I can
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<td>1 get more comfortable -- or not more comfortable -- 1 firm, nobody literally -- and maybe I am exaggerating, 2 where I think we should be looking is where those 3 incentives need for the long term. 4 Now, there the -- that's called the lower income, 5 lower net worth accredited investor, or somebody who is 6 a non accredited investor by today's definition gets a 7 great deal of comfort that they are actually investing 8 pari passu alongside long sophisticated money. 9 JEFFREY SOLOMON: Uh-huh. 10 CHAIRMAN JAY CLAYTON: For me, just speaking 11 personally, I take much more comfort that I am 12 investing alongside somebody who is putting their 13 money pari passu with mine, than -- that I have enough 14 money to lose. And it's -- I think we need to change 15 the paradigm a little bit from one that's dealing with 16 a distribution model to one that's dealing with a 17 co-investment model. 18 WILLIAM HINMAN: And not surprisingly, you know, 19 we ask that specific question in the -- in the 20 harmonization release. I wonder where it came from, 21 but, you know, that approach as well as thinking about 22 vehicles through which non accredited investors could 23 invest, where there's a sophisticated intermediary, 24 where there's someone who either has co-invested or 25 has, you know, fiduciary obligations to the investor</td>
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<td>1 or ways to pool some of the smaller investors together 1 CHAIRMAN JAY CLAYTON: We -- we put tremendous 2 so the issuers that you all are looking out for are 3 not overly burdened by having high numbers of retail 4 investors, and those are all things we're looking at 5 in that harmonization release. And, you know, Jay's 6 last point is a good one. You know, if you have 7 someone there alongside you who is very sophisticated 8 investor and you're 15 percent of the deal, you're 9 probably pretty well protected, so we want to look at 10 those things. 11 YOUNGRO LEE: Yeah, I mean, the main point from 12 the committee perspective, we want to add value to 13 that conversation, and -- and to address the -- the 14 goal is, again, I am just going to focus on bringing 15 capital to non traditional markets and allowing it to 16 everyone. What I am saying is it's not just -- it 17 can't possibly be change -- just change the definition 18 of credit investors. It has to be holistic in how we 19 think about the entire investment infrastructure and 20 systems, and I think that's where really the 21 sophisticated investors, whether it's an investment 22 bank or -- or recognized brand name, CV firms, a 23 product firm taking a lead, but you have to create 24 incentives for them to want to do it. Because right 25 now if you ask every single legitimate investment</td>
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| 1 firm, nobody literally -- and maybe I am exaggerating, 1 but I feel like 99 percent will say no way in hell am 2 I accepting a non accredited investor because there's 3 no incentive. 4 So that's kind of where -- 5 JEFFREY SOLOMON: Or worse yet, if you do it and 6 there's a problem. 7 YOUNGRO LEE: Right. 8 JEFFREY SOLOMON: So that -- and that's -- this 9 goes to something I think -- I am largely in agreement 10 with what you said. Here's the challenge. Every time 11 somebody loses money, it's -- it's not in their own 12 mind because they made a risky investment, it's 13 because somebody did something to me, and -- and 14 that's the knee-jerk reaction. And I'll say even in 15 the public markets, you know, when we have all these 16 protections and we're underwriter and we have all 17 these responsibilities, as soon as something goes a 18 little bit -- you know, as soon as anybody loses a 19 little bit of money, everybody is just -- you know, 20 everybody is getting sued. 21 CHAIRMAN JAY CLAYTON: Well, and the public 22 market are, and will remain a distribution model, 23 right? 24 WILLIAM HINMAN: Uh-huh. 25 | 1 CHAIRMAN JAY CLAYTON: We -- we put tremendous 2 liability on the issuer and the underwriter at the 3 time of an IPO because the underwriter is out, the 4 issuer is dis -- and it -- and the people they are 5 distributing it to by and large do not have the 6 ability to kick the tires 7 I -- I do think that the private markets, which, 8 you know, weren't around in any way, shape or form like 9 they are today when we develop the accredited investor 10 model, and they weren't around really when we developed 11 the -- the private markets have developed to not be as 12 much of a distribution model, and our distinction 13 between how main street investors invest in the public 14 and private markets hasn't really evolved with that 15 change And I think what you're saying is let's 16 recognize that there's probably some holistic 17 development that need -- you know, changing the -- 18 changing the level from $300,000 to 500 or 100, or 19 changing the net worth from 1 million to 500 or 20 excluding That's not really going to solve the 21 problem 22 MARTHA LEGG MILLER: I'll -- I'll jump in here 23 for the first time today. It's been really fun, this 24 meeting, to let Carl and Jeff do all of the leg work 25 of leading the meeting, unlike last time, so --
JEFFREY SOLOMON: You mean Carla just to be clear.

MARTHA LEGG MILLER: You've done a wonderful job, and I am very grateful for your leadership. I think that this is really probing the session that we started the day with. I think it's nice that it's almost bookends, that we started out talking about thinking big thoughts about how the market could and should work, and the context of questions that are teed up in the harmonization release, and I think what we're discussing really goes to the heart of how does this committee think that the rules could and should be changed to work better? Looking at the way that the market has evolved, there are big questions, and that's a big topic. That's a lot to tackle, but I feel confident that we're in good hands given the wealth of experience that each of you brings from very different areas, and so I just -- I am excited to see the ways that we take the different experiences. You know, Youngro, you're talking about one set of experience, but you have the -- you know, you have seen lots of different areas that are focused and Crowdfunding.

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You've got Jeff in another area looking at a totally different segment, but I think it is the confluence of these perspectives that's going to really provide for an enriched discussion particularly when we meet next and we start really delving into the harmonization release, but I just -- I want to encourage all of the Committee members to -- at the same time that you think on very micro levels of does the acc -- you know, does the accredited investor definition technically work the way that we think it should thinking more broadly about the entire construct that we are dealing with, the pooled investment vehicles with individual investors who back them, and with the companies that we are interested in supporting as they grow in scale. So I just want to encourage the breadth of thinking on this because it's -- it's the type of thing that it gets me excited, it's the reason that I love what I have the opportunity to do at the SEC, and I think it's the reason why each of you were interested in serving on the committee, it's to get the think big thoughts, and to shape how the rules work.

CARLA GARRET: And I'll say just to follow up on what we talked about earlier about framework for the November meeting and the harmonization rules. There ---

And then the second is should there be different designations?

And I don't know how you measure this, but based on either capital at risk that's -- that's put in place by the fund managers, and would that create a distinction. And so those are two levers that I don't really see. They -- they don't exist in terms of regulation, but in terms of the way that the private market operates they do exist because a large LP when they are evaluating a fund, they want to know how much the GP is putting in the fund, it matters to them, and it matters so they are not just how -- what the size of the check is, but what the size of the check is relative to the net worth that they think that person has because it says a lot about the competence they have in the product, and I think that there's some element of that could float through from a regulatory side too, but I don't know how you think about encoding that, but I am just trying to think big picture, like, what are some of the levers that haven't been used.

WILLIAM HINMAN: That's where -- you know, that was the point of the co-investment point.

JASON SEATS: Right.

WILLIAM HINMAN: And we're going to be looking at
it, and give -- we'll look forward to the committee
side of that.
Actually, tomorrow is a panel on the harmonization release, has some folks that have been thinking about some of those issues. I think they will be pretty informative, whoever is participating in the subcommittee here may want to listen to that panel tomorrow because I think they have some ideas along those lines.
JASON SEATS: Uh-huh.
CARLA GARRET: Does anybody else have other items that they'd like to discuss?
Okay.
JEFFREY SOLOMON: So on the subcommittees for the harmonization from the first discussion we had, are we going to have a separate sort of -- I mean, this is a good subcommittee that's going to deal largely with investments and private companies and maybe venture -- more venture oriented. We had talked a little bit about maybe sort of trying to take on some of the pooled investment vehicles that were outside of that.
I just want to make sure, are we having two subcommittees or one?
CARLA GARRET: I think right now we're starting with one, and then we'll also talk about -- we can talk about speakers and people that we could have address the full committee. That might be a good person to have a speak talk about the difference for the full committee.
JEFFREY SOLOMON: Great.
CARLA GARRET: Okay. Thank you to everybody. I think this has been a great meeting, and thank you so much for coming to Omaha. Our next meeting is November 12th, it's in Washington, DC. As you know, we'll be focusing on the harmonization release, as we have been talking about. Thank you to the SEC staff, thank you to the chairman and the commissioners for being here, and with that I adjourn the meeting.
(Whereupon, at 3:27 p.m., the meeting was adjourned.)
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