RECORD OF PROCEEDINGS

SECURITIES AND EXCHANGE COMMISSION

ADVISORY COMMITTEE

on

SMALLER PUBLIC COMPANIES

First Day of Meeting

June 16, 2005
1:00 p.m.

Columbia Law School
435 West 116th Street
New York, N.Y.
The following individuals were present in person:

Committee Members:

Patrick C. Barry
Steven E. Bochner
Richard D. Brounstein
C.R. "Rusty" Cloutier
James A. "Drew" Connolly III
E. David Coolidge, III
Alex Davern
Joseph "Leroy" Dennis
Janet Dolan
Richard M. Jaffee
Mark Jensen
Robert E. Robotti
Scott R. Royster
Kurt Schacht
Ted Schlein
James C. Thyen
Herbert S. Wander

Committee Observers:

George J. Batavick
Daniel L. Goelzer
Jack E. Herstein
SEC Staff:

Cindy Alexander
Anthony G. Barone
Mark W. Green
Gerald J. Laporte
Kevin M. O’Neill

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MR. WANDER: Good afternoon, everyone, and welcome to I guess our second public meeting of the SEC Advisory Committee on Smaller Public Companies. I'm co-chair of the Advisory Committee, Herb Wander, along with my co-chair James Thyen, who is sitting next to me and we, as I say, welcome all of you.

I'd like to start off by thanking our hosts from Columbia Law School for their hospitality, which has been fabulous. We had subcommittee meetings this morning, and they were in very nice locations with coffee and rolls and everything else, and we had this very nice meeting room.
for this afternoon and for tomorrow morning's hearings and, again, thank you to everyone at Columbia for all their help.

I think it would be appropriate if we went around the room and just introduced ourselves to our audience, and it's not only our audience here in the meeting room, 105, but it's also the audience that is on the web page.

So I'm going to start with Dick Jaffee, if you could just give us your name, your company affiliation and city, I think that would be helpful to everyone.

MR. JAFFEE: Sure, Richard Jaffee --

MR. WANDER: Excuse me, you have to press the button.

MR. JAFFEE: Richard Jaffee, Dick Jaffee. I'm chairman of the Board of the Oil-Dri Corporation, a New York Stock Exchange smaller publicly traded company and we're located in Chicago, Illinois.

MR. JENSEN: I'm Mark Jensen, I'm a partner with Deloitte & Touche.

MR. BATAVICK: I'm George Batavick, I'm a member of the board of the Financial Accounting Standards Board, Norwalk, Connecticut.

MR. DAVERN: My name is Alex Davern, Chief
Financial Officer at National Instruments, audit committee of SigmaTel, Inc.

MR. BROUNSTEIN: I'm Rick Brounstein, I'm Executive Vice President and Chief Financial Officer of Calypte Biomedical out in northern California, in Pleasanton.

MR. BARRY: I'm Pat Barry, I'm the CFO of Bluefly.com.

MR. GOELZER: I'm Dan Goelzer, I'm a board member of the Public Company Accounting Oversight Board in Washington, D.C..

MR. ROystER: Scott Royster, Executive Vice President, Chief Financial Officer Radio One, NASDAQ-listed company located in Washington, D.C.

MR. SCHACHT: I'm Kurt Schacht with the CFA Centre for Financial Market Integrity, previously in Charlottesville, Virginia, but as of two weeks ago we're now in New York City.

MR. ClOUTIER: I'm Rusty Cloutier from Lafayette, Louisiana. I run a small bank called MidSouth Bankcorp. We're located in Louisiana and in the State of Texas.

MR. SCHLEIN: I'm Ted Schlein, one of the
managing partners of Kleiner Perkins Caufield & Byers, a
venture capital firm in Menlo Park, California.

MR. CONNOLLY: I'm Drew Connolly, President of
IBA Capital Funding, a capital funding specialist firm in
Perrineville, New Jersey and the Executive Director of the
CEO Council.

MR. ROBOTTI: Bob Robotti from New York City
with Robotti & Company. We're registered broker dealers,
investment advisers, investing in small cap, microcap
companies.

MR. HERSTEIN: Jack Herstein with the Nebraska
Securities Bureau, Department of Banking, and here as an
official observer.

MR. DENNIS: Leroy Dennis, Executive Partner of
Audit Services for McGladrey & Pullen, a CPA firm
headquartered in Minneapolis, Minnesota and I also serve on
the Executive Committee for the AICPA Center for Public
Company Audit Firms.

MR. BOCHNER: Steve Bochner, a partner at
Wilson Goodrich, Sonsini & Rosati, a law firm located in
Palo Alto, California.

MR. THYEN: Jim Thyen located in Jasper,
Indiana, President and Chief Executive Officer of Kimball
International, a diversified manufacturing company.

MS. DOLAN: Janet Dolan, President and CEO of Tennant Company, a NYSE-listed company headquartered in Minneapolis, Minnesota.

MR. COOLIDGE: Dave Coolidge, Vice chairman of William Blair & Company, investment brokers and money managers located in Chicago.

MR. LaPORTE: I'm Gerry Laporte, I'm Chief of the Office of Small Business Policy, which is providing staff support for the Advisory Committee.

MR. WANDER: Thank you all. And I'm now going to call on my co-chair Jim Thyen for some introductory remarks.

MR. THYEN: Thanks, Herb. Some building thoughts from what Herb said.

We were formed about 45 days ago, 50 days ago. Our activity has been high since then, it's been very meaningful, very focused. I believe our structure of subcommittees is working effectively and it's easy to see the teamwork and collaboration that we are building. We're a diverse group, diverse in experience and background, diverse in viewpoint, yet our professionalism has blended well and that's really why we were asked to serve, so I
really want to thank you for your time, the talent and the
mind share you've given to this very important activity.

Another comment about sponsorship. As
expected, any journey has changes, it has challenges. I
believe when you're leading a journey of change like we are,
we're actually leading a committee and we're going to be
faced with unexpected changes and they can be viewed as a
cause of concern or a source of opportunity. Clearly, we're
going to lose one of our committed sponsors in Chairman
Donaldson, but the indications are we will gain an equally
committed sponsor.

We know the desire, the continued commitment of
our other sponsors, Director Allen Beller and Chief Gerry
Laporte, remains very high and very strong, so we should be
grateful for Chairman Donaldson's role in bringing us into
existence and let us remember that our charter is
established, our agenda is framed and our end goals and our
priorities remain unchanged. And so we're going to continue
with your leadership and with your constructive mind share
to do this productive work, regardless of what change is
above us.

A few comments about the size committee.

You're aware that from the communication that we are formed,
we are organized, we are active. We are composed of members of the subcommittees. Our activities have been shared with the subcommittees and the subcommittee chairs. Besides being a member of each subcommittee, Herb and I are serving on the size committee. Our intent will be to adjourn the size committee upon completion of our assignment and we believe that is a recommendation to this full Advisory Committee of a solution for determining the definition of a smaller public company. That's the course we're on.

We believe there's an additional outcome, which is to provide the deductive reasoning that supports the recommendation and the logic points that will support the recommendation for definition of a smaller public company, and we believe the work to date is starting to give you a framework with some clarity that you can use in your subcommittees to calibrate against for the regulatory change recommendations that you will bring forth to this committee.

So we're engaged in moving in and hopefully that communication is flowing, and you've got a framework of where we are headed. We know that's an important foundation for the work each subcommittee is doing.

Thank you.

MR. WANDER: Thanks, Jim.
As Jim said, we began our work in April of this year. We have divided the full committee into four substantive subcommittees who will each give a report shortly to the full committee and to those in attendance. And those are the Capital Formation Committee, the Accounting Standards Committee, the Corporate Governance and Disclosure Committee and finally the Internal Control Over Financial Reporting Committee.

These subcommittees meet by themselves, Jim and I try and attend and there's an observer from the SEC to help them as well, and all of the members and all of the chairs of the subcommittees meet with Jim and I on a periodic basis to go over open issues, direction, focus and to keep in touch so that we have a lot of communication among us.

I will say that I think we're still in the initial stages of our journey. I think we're making very, very substantial progress based on the reports that we've already been given, as well as the reports that you will hear today, and from attending some of the subcommittee meetings this morning. So we are making a lot of progress. We hope to keep on our time schedule that has been published and we hope that our next meeting, which will be in Chicago,
Illinois on August 9th and 10th, we will have actually some formal recommendations for the whole committee to consider. We will also be meeting in September in San Francisco. We hope to hold hearings again both in Chicago and in San Francisco, because we want the broadest public comment to us on both our agenda, items that we have perhaps not included in the agenda and get as much input as we can.

And now I'm going to move into a review of the comments received on our agenda.

As you know, we published our agenda in the Federal Register and we have received approximately 30 plus comment letters. Each of these has been posted on our web page. We hope to be very transparent, and so all of you can monitor those comment letters. We believe they're very valuable and we continue to solicit comments from interested parties on our agenda, as well as interested parties who might like to appear and provide oral testimony or oral observations to us. We have a number scheduled tomorrow morning and those are listed on our agenda, and we will hear more in Chicago and in San Francisco.

Of the comment letters that we did get back, I just would like to raise some highlights with you, not to take you through all of these. But I will start with the
fact that a number of I think the responders felt that our
agenda was too ambitious, that perhaps we should prioritize
those areas that are in higher need of refinement, and focus
our efforts in those areas, and we will take these comments
into consideration and we in fact have essentially talked
with our subcommittees to make sure that they have focus on
three or four items at most so we do not try to be too
ambitious and only skin deep in our analysis.

A number of the commentators also reported on
what they believe the definition of a smaller public company
should be, and those will be very helpful in determining the
recommendation that our special ad hoc size committee under
Jim's direction will make recommendations hopefully that we
can adopt and those letters were extremely helpful, and
interestingly, without knowing what's been on our internal
agenda on those issues, they are very close in point to what
we've been thinking about.

A second area that I want to mention is
coverage by analysts. There will be a couple of people
testifying tomorrow about that issue. We're greatly
concerned that there is enough independent, first-class
research about public companies, including smaller public
companies, if that's at all possible. And indeed, yesterday
morning I was awakened by some research that came on my fax machine all the way from Russia, touting a particular company. This is not necessarily the kind of research that we're trying to encourage, but that's an agenda item that I think we will be examining.

The next area, of course, is the sort of blockbuster, the internal controls under Section 404. We received letters from a number of company executives, we've received letters from a number of the Big Four accounting firms, as well as BDO Seidman. Again, I think those have been helpful not just in dealing with the direction that we might take in terms of internal controls over financial reporting under 404, but also dealing with accounting standards, how they're adopted, when they're implemented, and whether there should be differential accounting for big companies versus small companies or whether there should be any special recognition of the needs of smaller public companies.

Capital formation for very small companies, and I say very small companies, most of the comment letters that we have received in this area really deal with sort of mini microcap companies and the need to continue to have those companies as viable players in our economy, but also to have
them provide investors with the kind of information that helps nurture a good capital market and provide protection for investors under the SEC's mandate under the securities laws.

We also, Rusty had a couple of comment letters from smaller community banks, who not only talked about their size, their needs, but also indicated a fact that they're regulated by a number of other sources and perhaps they're overregulated in the sense of having double, triple, quadruple regulation and some sort of regulations by the banking authorities, for example, suffice or fill some of the void of regulation.

I went through just briefly these letters to tell you, to make sure that you realize that we are reading them and trying to analyze them and they will go into our thinking, and to continue to encourage people to provide us with additional information, either through testimony or through comment letters. And again, as I said, those will be all posted on our web page.

Having finished that, I would like to move to the real heart of our meeting here today, which is a discussion of the reports on the activities of our subcommittees, and I'm going to start with Janet, to talk
about internal control over financial reporting.

MS. DOLAN: Thank you very much, Herb.

First of all, I want to thank all the members

of our subgroup, as well as, we have terrific representation

both from the PCAOB and the SEC and I think their

involvement in our work is very helpful. We avoid the "we

have a discussion then we go find someone and then we come

back." It's very helpful having everybody in the room

together.

We have had very what I would call spirited and

not yet unanimous debates and discussions, but we are on

exactly the path that we laid out when we were at our first

meeting, and that is, we laid out as our charge that we want

to see if we can provide advice and guidance and

recommendations in such a way that we insure and maintain

the investor confidence that 404 was intended to produce,

and yet can we make recommendations that will significantly

reduce the cost and the time that companies, particularly

small companies, are incurring in order to fully implement

404 as it is in its current status.

So it's that trying to strike the right balance

between both of those that we consider our charge. And we

laid out as a framework for how we would go about this

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looking at factors which we would call risk factors; are there ways that we could provide some guidance and recommendations whereby we would bring some risk assessment to bear so that 404 does not continue to be a one size fits all, but can we provide some guidance whereby we keep the emphasis on what's most important, but help highlight what is less important and do it in some way that reduces the implementation burden.

So we divided ourselves into four subgroups but three that actually go to the risk factor and that is, first of all, just a subgroup looking at what are some different ways that we could segregate different controls that require to be attested and segregate them into different buckets depending upon the risk factor.

The second is could we do something around the timing, which is could we have a variable implementation in some way that less important or less critical controls might be evaluated and attested to on a more periodic basis or perhaps we divide the work in such a way that all the work doesn't have to be done at the end of the fiscal year. So are there things around when things happen that we can spread the work around and therefore reduce the cost and burden.
The third factor we call autonomy, but it goes to are there ways that we can identify things that could be done more by the company and relied on by the audit firms as opposed to requiring the audit firms to, again, test and attest to all controls as though they were all the same.

So as you can see, there are kind of three different elements of the whole risk factor. And so we have three groups working on that. We heard from them today and we're all working together to support them, but we have three separate groups leading the charge on each of those three.

Our fourth one is actually more of a separate one, which is are there any particular special needs situations, just as a company is going public or it's in its first year or two of being public, are there just certain circumstances in which a company, while it may fall into a certain size category should be treated differently because of some other factors or circumstances surrounding it. So we heard today and we are looking at different opportunities in each of these areas.

We are also very interested and cognizant of the SEC and PCAOB pronouncements that came out in mid-May subsequent to our meeting in April in Washington, and we're
very interested in looking at those and seeing whether they
have provided some of the relief that we're looking at or
can we build on what they've done to more fully define and
perhaps give more concrete foundation to the work done so
far by both the SEC and PCAOB in this effort to try to
create more of a risk assessment and more guidance for the
audit firms in terms of what is the appropriate level of
auditing that should be done, based on the needs of a
particular company.

We also identified additional meetings which we
will have, we will be advancing our work significantly by
the time we meet in August in Chicago. We identified
additional information which we need which the SEC will be
providing and other organizations that we will look to to
provide us more input.

Then the last thing we did is that we also
discussed whether we should take a position on extending the
current moratorium that exists for very small companies.
There still are about 4,000 companies that have not done
their, been required to have their 404 certification yet.
Our recommendation is that no more companies be required
until we finish our work and until we have greater clarity
on the results of this team as well.
So we are just as a subgroup, we're making that recommendation to our bigger group that we at least consider that. And I think that is a roundup of what we got done in our short but lively meeting this morning.

MR. WANDER: The recommendation I believe was unanimous that in effect the postponement continue for another year while we can get our hands around 404 and as well as the COSO committee could get its report out, they have a special committee dealing with small companies.

We will probably bring this to a vote in August. We do not plan to bring this to a vote today, but we thought it appropriate to say where the subcommittee has decided to seek relief at least on this temporary basis and let you all know about it so that you can be thinking about it, we will probably be discussing it among ourselves prior to our August meeting.

Are there any questions or further comments concerning the internal control of the financial reporting?

MR. JAFFEE: I just want to nail down what you're saying. We're going to bring to a vote in August to recommend to the SEC that those people under 75 million get another year or delay implementation until we complete our deliberations or what, do you think? Or do you know?
MR. WANDER: I don't think we had really decided. I think that's really based on the subcommittee recommendation, but our life is probably over early next year, so I would think a one-year postponement would be more appropriate than an indefinite, but that's something really for the committee to really discuss and debate and determine. But we thought it appropriate just to mention it, because it's coming up very fast and a number of people in their comment letters have clearly asked for that postponement.

MR. CONNOLLY: Herb, just very quickly. So I'm clear on that, the non-accelerated filers who are due to be phased in are going to be getting, based on our recommendation presumably to be passed, a full one-year phase-in period beginning -- and that's going to be a quasi recommendation, not currently voted on but certainly floated to the top with the new chairman being sworn in July 1st being aware of that?

MR. WANDER: What I would expect is, let's assume it's asked for a one-year delay from what is it, July 15th of this year to, for the first fiscal year ending after July 15, 2006. If we make a formal recommendation, it will be written up and we'll have some basis for making the
recommendation and it will be delivered to the five
Commissioners, assuming that there will be five SEC
Commissioners at that time, and how many ever are sitting,
and we will also, obviously, give a copy to our friends at
the PCAOB and then we would hope that the SEC, the ball
would be in their court. We hope they would act favorably
on it if we recommend it.

Any other questions of Janet? Any other
thoughts on internal controls?
If not, let's go to Dave Coolidge and Capital
Formation.

MR. COOLIDGE: We met this morning and again,
thanks to everybody for attending and participating. We've
had a lively discussion. I think we have some specific
thoughts. These aren't in the form of formal
recommendations, but things that we are thinking about.
There are a number of items that really do pertain to other
subcommittees and so many of this comes in the form of a
suggestion to the other subcommittees to think about our
thoughts.
Number one is with respect to the independent
director issue for companies. These are primarily listing
standards. Our committee's feeling is that the pool of
qualified people has shrunk and is shrinking due to a
variety of items, one of which has to do with the definition
of an independent director. Now, I know these definitions
were wrestled out and agreed to, but there's a feeling that
they might be reviewed again to loosen up a little bit so
that more people could be qualified as independent
directors, so that the pool would be expanded as opposed to
shrunk as a result of past work.

We also, I think, feel that the definition of a
financial expert is very tight and tough, and perhaps that
could be looked at again for the purpose of qualifying as a
financial expert on the board.

One issue that we are somewhat mystified about
is why affiliates defined generally as 10 percent
shareholders or greater are not deemed to be independent
directors for the purpose of audit committee attention. It
just seemed to us that that was a difficult -- we couldn't
quite understand the logic of that, and whether that ought
to be revisited or not, either have a higher threshold or
just ignore it altogether, what is the conflict between
being independent and owning a lot of shares, we can't see
it, so that's for discussion at a later date.

With respect to the size committee, we have a
feeling that a revenue test, an asset test ought to be
looked at very hard, in addition to a market capitalization
test, which has been sort of the traditional approach the
SEC has used to defining break points for whatever filing
regimens or other size-related issues. We think that
revenue and assets reflect the complexity of a business,
especially as it relates to 404 type of attestation issues,
revenue and assets reflect really the complexity of business
much better than the market capitalization definition, and
it doesn't mean that they have to be mutually exclusive,
perhaps there could be both a market capitalization test or
a revenue test so that you could qualify for relief based on
either one.

In terms of trading activities and markets for
stocks, I think there is a concern in our committee's part
that a lot of the small companies are in a position where if
they don't qualify for the New York Stock Exchange or for
the NASDAQ listing, they are generally on the bulletin
board. The bulletin board as we understand it, is an
activity that the NASDAQ maintains, really because of an SEC
mandate. It's something that the NASDAQ would probably like
not to have to run and that's because they're a for-profit
entity and this is not a for-profit undertaking for them.
There are no listing fees coming from the companies that are traded on the bulletin board, and I guess we're wondering whether or not it wouldn't make sense to ask if we're going to continue to force the NASDAQ to keep this market going and the SEC, perhaps they should be compensated for that with a modest listing fee from the companies themselves.

We know the NASDAQ and we'll hear from one of the NASDAQ representatives tomorrow, we can quiz him on that. They were looking at forming something called BBX which would have been a listing activity. They went out to Bulletin Board companies, surveyed them to find out whether they would be interested in supporting such an exercise and they were underwhelmed by the response, and we suspect that's because if you're trading on the Bulletin Board as a company you don't have to pay anything, but if you were to go on BBX you would have to pay something and the companies said "Why would I want to do that" and perhaps subject yourself to some more oversight by the NASDAQ.

But this is something that we think is an issue, because if the Bulletin Board were to go away, the only other venue is really the Pink Sheets and that is not an electronic activity and it's more cumbersome and would reduce trading and increase liquidity. So I think we're
thinking about seeing whether or not there's a way of making
the Bulletin Board a more viable business enterprise, which
probably means some kind of a listing fee from those that
are traded on the Bulletin Board.

With respect to, and this really gets into
Janet's committee's work and it's along the lines of the
timing of especially attestation and 404, our thought was
that for small companies, however we defined them in our
size committee, that this only has to be done every three
years. This would reduce the cost pretty dramatically if a
company went through the process, and didn't get the 404
attestation and they corrected whatever deficiencies were
cited, that they be given a two-year pass, have to come back
at it subsequently. We think this would reduce the cost and
burden tremendously, but the benefits to the investors would
be there, because everybody would have to go through it
initially, and then control systems would probably be
improved, which is good, but is it really necessary to ask
these small companies to do this every year.

So that's an idea.

Also, along the lines of materiality, we think
that not only is materiality important with respect to
bringing the 404 look-see at everything in terms of internal
control, should be a materiality test, but it should also be
consistent. I think we've got some evidence that there's
inconsistency between auditing firms and, frankly, between
offices of the same auditing firm as to what's material and
what's not material, and hopefully we can get to tests with
respect to materiality and also consistent across all the
auditors.

There was another thought and we don't know if
this is feasible or not, but whether or not competition for
404 attestation could be developed. At the present time the
auditing firm that audits the books of the company does the
404. Is it possible to define the 404 auditor to include
someone else other than your own auditor, which would
perhaps allow you to perhaps bid the 404 attestation work
out, introduce a little bit of competition. Don't know if
that's really feasible or not, may not be practical, but
it's a thought to, again, on the cost side, to try and
reduce the cost of that process.

Some fairly minor -- actually I shouldn't say
minor, because to some people they're really important, but
we found some rules we think we're going to come forward
with on rule change ideas. Rule 701, which has to do with
companies being required to provide financial statements to
employees who exercise options if there are more than 5 million a year of options granted, there was an idea perhaps the 5 million threshold was too low and it ought to go up. We're thinking about 10 million, but that's to be debated.

There's a rule, 12g5.1, which counts shareholders of record for the purpose of being a public company. There was a thought that the current threshold of 500 shareholders was a little low and also that the concept of counting shareholders of record is not necessarily the right way to do it, because you have beneficial shareholders behind those shareholders of record and people can game the system and shrink down their number of shareholders if they want to stop reporting, so the idea would be to adjust the levels of shareholders, but through the beneficial shareholders, as opposed to continuing to look at shareholders of record.

Another point and I should have brought this up actually under the 404 discussion in terms of materiality, the expensing of stock options as we know has been a very widely debated subject, but in smaller companies where this becomes a material expense item, it lowers net income, perhaps, for these companies, by a reasonable amount, and then you start judging materiality as a percentage of net
income for the purposes of 404 looks.

We thought it might be a good idea to add back stock option expense to the earnings stream and then determine whether something is material, because these charges can be and have been pretty material to some companies, but it lowers their net income by such an amount that then for other materiality tests everything becomes material because their net income has been reduced by a lot, but the thought was perhaps to add back stock option expense to whatever metric is being used for determining what's material and what's not.

An additional subject that we've talked about is the whole area of Regulation SB. It has a $25 million market cap threshold now, which makes it available to small companies. In our view that's a very small company, and if we redefine what a small business is in terms of this committee, should we be thinking about applying Regulation SB to all additional companies or some subset of all these additional companies, presuming that we're looking at the definition of small companies which is much larger than the $25 million number.

So that's a whole different subject to get into and debate, but if we're going to define small business in
this committee for a variety of purposes, we all agree, the
Commission agrees, should we be using that same test for
other small business rules within the Commission, especially
the registration statement process which has now Regulation
SB and Regulation SK and should the SB registration option
be available to everybody that we define as a small business
for purposes of this committee.

And there is another small rule issue that we
looked at, Rule 15c2-11 which involves brokers being
required to file what's known as a 211 statement in order to
start trading in a stock, and those are disclosure
statements with respect to those companies, and I think that
the view is if you're going to allow brokers to trade these
stocks and they are going to be actively traded, that those
disclosure statements be made available to the public, and
as we understand it, they're currently not available, and to
ask the companies that are involved in that activity to
update those filings on an annual basis.

That's a long list, some of which are much more
impactful than others, but these are the things we looked at
and are discussing. No final recommendations, but just want
to get them on the table for everybody's consideration.

Thanks.
MR. WANDER: Sounds like you were very busy this morning. Are there any additional comments or questions?

MR. DENNIS: I have a question. This is Leroy Dennis. Just on the size comments that you made. Our committee has also discussed a lot along the size with our representative from the size committee. Our thoughts are aligned with yours in that we believe that, we actually believe there ought to be three levels of companies that have different rules applied to them; one being larger public companies, the other being what I'll call the middle, which maybe we would allow some relaxation in the rules, but then you look at the traditional SB company filers, which are 25 million and whether that's 25 million or whether that's 50 million, but what I would call very small companies, I think we could, with a size breakdown like that, we can maybe get much more aggressive, at least on my committee, with the accounting recommendations for a company with 25 or $50 million market cap as opposed to a company with 500 or $700 million market cap, because those are clearly different levels of expertise and different levels of needs by the users of those financial statements, and I think if we just went from a 700 million or a 500 million
down, and put that all in one bucket, we'd have a whole lot
of really smaller SB filers that would still be overly
burdened for what their users want and need.

So we would support you and I would ask that
the size committee look at whether there should be,
effectively should we take the SB filer to keep that SB in
place, take that to a certain level, whether it's 25, 50
million, whatever that number is, and then have a middle
tier that maybe is more of the focus of this committee.

MR. THYEN: This is Jim Thyen. Leroy and David
both, we hear you, and we will take that under advisement
and discuss it at our next meeting.

MR. JAFFEE: I had a question for Dave, because
I think he's in a very good position to respond to this.
This is a question that we discussed this morning. Capital
formation. Are you seeing a reduced number of companies
wanting to go public or willing to go public because of
these regulations or are IPO's going on apace, and is that a
bad thing if it is reduced?

MR. COOLIDGE: I think the average size of the
company going public has increased in terms of market
capitalization, certainly the average size of the
transactions has been increasing. This is driven in part by
the marketplace. Institutional investors on average have a
lot more capital to invest, so they're not interested in
looking at very small companies, very small deals, so that
there's just sort of a market push for larger companies and
larger deals.

I think also, though, on the issuer side there
are companies without question who are reluctant to go
public because of the additional cost burdens of going
public, so they have to be bigger, it has to be a better
value proposition before they're willing to jump into the
public markets. There's just a lot more hurdles to get over
and there's a lot more expense to be incurred in order to
become a public company today as opposed to five years or
ten years ago.

So the answer to your question is yes, I would
say there are fewer -- it's hard to say, there are fewer
companies, because when the markets are receptive, there's
lots of companies going public and when the markets are not
receptive, there are very few companies going public, so you
can't look at annual data and get any real feel that because
a regulation went in, that stopped companies from going
public. It's primarily driven by the marketplace and the
demand for new issues.
But I'd say that in general the size of a company going public today in terms of market cap or revenue or whatever is much bigger than it was five or ten years ago, because of the increased costs of entering the public market and also because the public market, especially if you're going to have a full blown institutionally supported deal, requires a bigger deal, more float is being required by the Investors, so that means a bigger deal, that means a bigger company.

MS. DOLAN: This is Janet Dolan. I just want to make a followup comment on the size. I think each of the subcommittees did spend time this morning responding to some of the proposals coming out of the size committee, but I think our committee and I would suspect the other committees probably had the same reaction, which is while we could generally give feedback on what we think a general size limit might be, until we see the proposals that come out from each subcommittee, we can't agree that that's the "one size fits all," if you would say, standard. There might be some recommendations that we like, but we would only apply them to a much smaller category. So I think all the subcommittees are sort of
dealing with the same thing, which is until we see all the
recommendations, we can't say that we would agree that those
recommendations should all apply to only one size of
company. There might be some exceptions.

MR. WANDER: Any further comments? Yes,
Leroy.

MR. DENNIS: Herb, one other comment I'd like
to make. On your comment on competition, and I'm not sure
it's part of this Committee's agenda, but I want to make it
anyway. As far as increasing the competition for 404
auditors and driving the pricing down on that, it seems like
the bigger issue I think we've got to deal with in the
United States is we have something above 700 registered
public accounting firms in the U.S. and effectively four do
97 percent of the public companies out there, and there
needs, if there's a way we can get more acceptability of
those smaller companies to accept smaller local firms that
are registered, and inspected by the PCAOB, that provides a
lot more capacity into the system than there is today and a
lot more competition in the system than there is today, than
we have right now.

I don't know where exactly that gets addressed
or if it should be addressed by this Committee, but I see
that as the bigger issue in the competition side of the 404 side of things.

MR. CONNOLLY: Just to respond to that very quickly, it's not what I was going to say, but we did think about that in terms of the potential 404 auditor attestation role, and it's pretty clear that the public company executives and certainly the marketplace participants are almost unanimous that they will not see a situation where a company that currently isn't a Big Four would voluntarily -- in fact, I think we heard the comment, we'd pay more money not to have to switch off because the marketplace perception were you to change auditors is so universally negative that your stock is going to tank.

So the only way we saw to induce or introduce competition was to potentially bifurcate the role of one's auditor and one's attestation auditor, if you will. So we worked hard to find a way to make it fair, but also make it feasible.

Very quickly, to try to answer your question, Dick, I am not knowledgeable as Dave is on the IPO side of the marketplace, but I can tell you that the reverse merger business is very much alive and well, and those companies are largely very small, often exceedingly small, with the
possible exception of Archipelago and the New York Stock Exchange, which have just completed a reverse merger, interestingly enough. And in fact, it is the entry point, or almost the universal entry point for, for example, Chinese companies who are listing on the Bulletin Board are almost all reversed into what are shells.

So that's a whole different segment of this marketplace that I'm hoping to get some data from. I know that Dr. James Angel, who was on the Bulletin Board Committee, I haven't spoken to him for many years, at one point had that data on Bulletin Board-listed shells.

MR. WANDER: Those are all helpful comments.

Any other comments?

MR. ROBOTTI: I did have a question or two.

One of the comments you made about the potential phaseout of the Bulletin Board and the Pink Sheets as an alternative was the Committee's observation that the Pink Sheets is not an electronic forum. Maybe I misunderstood that. What did you mean by that? How do you understand the differentials between those two marketplaces?

MR. COOLIDGE: I probably shouldn't have said that. There are two different venues and there is some overlap, Bulletin Board stocks and Pink Sheet stocks are
often the same company.

Our concern was that the Bulletin Board, the Pink Sheets as we understand is a viable business, they do make money and so they're going to be around. The Bulletin Board, that's our understanding is that it's not the case and that the NASDAQ would like to exit that business, and so that's really our concern, is that, you know, to have two venues is better than to have one and we're worried that the Bulletin Board is maybe not going to survive unless something is done.

I mean, it can continue to function by virtue of the SEC mandate that they keep it alive, but that is really what the comment was intended to --

MR. ROBOTTI: I wanted to confirm that of course the Pink Sheets over the years have clearly significantly changed, and the form today, since we're active investors in both Pink Sheets and Bulletin Board securities, the trading mechanisms, the quotes, realtime reporting is relatively comparable between the two markets. It's a transparent market, the Pink Sheets today, which is vastly different.

Dick mentioned his company at one time was a Pink Sheet company and at that time the Pink Sheet was
actually a physical system; telephone calls, subject bids and offers, a market that was very nebulous. And that's not the fact today. As a marketplace and trading mechanism the two are relatively comparable. There's not a loss of liquidity, there may be a perception issue.

MR. COOLIDGE: Our view, we may be dead wrong, is that if the Bulletin Board were to go away, that would not be a good thing for capital markets. Maybe you disagree.

MR. ROBOTTI: On the -- you mentioned the 500 shareholder account, so I guess you're also potentially looking at the 300 shareholder account.

MR. COOLIDGE: They're linked together, right.

MR. ROBOTTI: Do you have, in that regard you say those numbers, 500 and 300 you're concerned about being potentially too low a threshold. Could you give me some kind of more feeling on that? Being an investor in that marketplace, I'm kind of of the opposite opinion that those are relatively good thresholds. A 500 shareholder account, 300 shareholder account are pretty broadly distributed securities with a lot of passive investors in them, so there's a logic for, gee, why that is a logical size. So I was curious about the thinking.
MR. COOLIDGE: The thinking went along the lines of, they're now shareholders of record, so you have a number of companies that are arguably below the 500, so they're not reporting, or they're not deemed to be public and not forced to publish. If we switch to a beneficial shareholder account, that would draw in a lot of companies now that are not reporting and perhaps don't want to, so if we were going to say we're going to go from shareholders of record to beneficial shareholders, wouldn't we move up the 300 and the 500 so as not to disadvantage those companies that aren't reporting and don't want to report to that extent.

Because we'll get pushed back clearly if we go from shareholders of record to beneficial shareholders, how do you balance that. I mean, you'd like them all to report--

MR. ROBOTTI: Not necessarily. Of course, I would say we probably have a huge problem on that part because the 300-500, that's a legislative issue, right, so we'd have to recommend some change. The definition of account is an SEC determination as to how to do account as opposed to the number itself is I think in the legislation. So I think there would be issues with that.
I still kind of think that 300 and 500 are pretty broad numbers that if we counted accurately that's probably a relatively broad standard that probably is good today, but that's a different issue.

MR. COOLIDGE: It's okay, you can come to our next committee meeting.

MR. ROBOTTI: The last issue is you did reference the Rule 15c2-11 deal and the concept of attestation on the part of dealers. I'm curious what your thoughts are on that area, because again, it's a subject area of some issue and concern to us. It is a little bit of a difficult issue.

Obviously, the companies would have no mandate over them to force disclosure of information and I think the SEC, their first mandate here, of course, is to protect shareholders and to enable companies to not provide data and therefore avoid a market transpiring in their security or to chill, doesn't serve a beneficial effect to shareholders.

So I'm kind of, how do you, what's your thought on that subject and what do you think about that rule and what are you looking for in that area?

MR. COOLIDGE: Well, as we understand the rule, the dealers are filing these 211 forms which do contain
disclosures about the companies they're going to trade in, and then before they're permitted to trade, the NASD has to say, okay, you've got enough here to begin a market. The idea was for those disclosures to be made public and for them to be updated annually and probably by the companies themselves.

Now, that may not be feasible, but that would be preferable to the system that they have today, which is the market gets started, yes, the broker has some information in his possession, but it may never get updated subsequent to the market being initiated, and nobody sees it. So I think we're on the same side of that question.

MR. ROBOTTI: The problem I have is there are shareholders who have a security who are interested in buying and selling the security. The company, we have no control over it, can't mandate disclosure on their part so essentially the companies can really chill any trading in their security at all by refusing to give information. I hear what you say, however, to terminate the marketplace, just like NASDAQ determining we're going to terminate the Bulletin Board marketplace because we don't know how to regulate it and it's a problem for us, to therefore eliminate the regulation of it doesn't serve the purpose. I
think that is the intent of the rule.

MR. CONNOLLY: Bob, this is Drew Connolly.

Just to feed into the thinking with Dave, on the 15c there
are two places, as you know, where that data is maintained;
it's the initiating broker dealer and then the NASD. The
NASD has consistently refused to release that information
and they simultaneously have a rule that brokers are
supposed to maintain current financial data.

So the question is where is the current
financial data. So we're looking at whether or not some
nudge towards broker-dealers being compelled to follow the
rule that exists, but also to give the companies some form
of obligation of annual disclosure, short of full reporting
and I certainly understand a lot of these illiquid
securities and smaller public companies.

We're very concerned that not raising that
number and not counting the number that are in DTC or Cede &
Company towards that rule is allowing a host of companies to
essentially buy back their stock, go private and
disadvantage the current stockholders. So we are concerned
about that and that really, I think, speaks to why we pretty
much unanimously would like to think about that.

MR. WANDER: Any further discussion? We're
going to have the General Counsel of the NASD tomorrow morning, as well as late tomorrow morning the CEO of the Pink Sheets, so think of all your questions and have them ready for Ed Knight and Cromwell Colson, because I think it is important both to have a market and to have information out there, and how to deal with that, as it's been pointed out, somebody will become a loser in either case, no matter what we do.

Why don't I go on.

Leroy, do you want to go next, please?

MR. DENNIS: Sure. Thank you. Our group, I think, had a very good meeting this morning. We've met several times via conference call since we last got together in Washington, D.C. I want to thank also the group that has been putting a lot of hard work in, and George and Patrick have done a great job and Tony and Alison from the SEC have been great support for us in our recommendations. So --

Kind of the same thing where Dave was headed, preliminary thoughts not yet to a recommendation stage, but I'll give you some ideas on what we're thinking about.

I talked a little bit about the size and we do believe that if we could bifurcate the size into three sections, where we really had a very small company and a
middle sized company and a larger company, would allow us from our accounting recommendations to make some possibly more aggressive recommendations on disclosure and accounting for those smaller companies than, say, if we had just a two-tiered system.

We'd also recommend that, if we went to a three-tiered, that we considered things like the quarterly reporting for a very small company, is that useful to the shareholders of a $25 million market cap company, or can there be some limitation on the disclosures that are done on a quarterly basis with a more robust disclosure and reporting on a semi annual basis for those companies.

Overall, we are not, we're pretty much, well, we are 100 percent in agreement that we would not recommend any different recognition criteria as it relates to accounting for small versus large companies. We think it does a disservice to the U.S. economy and is confusing to users to have different kinds of levels or different kinds of GAAP, so that a company that is smaller would report certain levels of net income versus a company that's larger.

To some extent GAAP is GAAP and I think we need to have some kind of consistent application across all companies in the U.S. in order to do a service for investors and allow
comparability.

Having said that, we think, and some comment was made in the comment letters regarding the same thing. We've clearly gotten into a system where simplicity is less of a consideration as opposed to possibly theoretical correctness in the accounting standards and we think that simplicity ought to be something not only in the accounting side, but I'd look to the size committee also and although I would agree that assets and revenues are a good measurement along with market cap, I think we have to weigh putting three or four factors into place with the simplicity and the ease of implementation.

A market cap measurement may not be perfect for everyone, but it's easy. And I think we need to move a little bit more towards simplicity or maybe a lot more towards simplicity in at least the accounting side of things and I think there's a lot of benefits that come out of that.

Some of the recommendations we're thinking about is that there be different transition rules for larger versus smaller companies as it relates to new accounting standards, and certainly new effective dates, or different effective dates, effectively allowing companies that would, the larger companies adopting it first would have the
resources to do things. The smaller companies having the
benefit of those larger companies and their auditors going
through that process the first year before they have to
tackle that, something similar to what we're doing with the
404 that's going on right now.

Probably one of the biggest areas we spent a
lot of time with, we feel that the biggest amount of pain
that's being felt by the system as it relates to the newer
accounting standards out there are not so much that, with
the requirements of the standard as they are with the
newness of the standard, and I know 123R is a favorite
topic of everyone. When we look at 123 that was issued four
to five years ago, and our belief is that people today have
a pretty good understanding of how that works and are able
to do that on their own, but maybe there needs to be some
transition rules for smaller companies that allow greater
auditor involvement in assisting in the design and
implementation of new standards that would not impair
independence nor impair a company's certification under 404.

So we're kind of thinking that for the smaller
companies there would be a, I'll say relaxation, that's
probably a bad word, of the independence rules related to
implementation of new standards, and for some period of
Having said that, we would also, again, if we went to a three-tiered system of smaller companies, for the very small companies there may be even a greater recommendation to have even greater auditor involvement in the design and implementation of their accounting, recognizing that they probably don't have the talent internally to do that, and going outside is an expensive process for them.

From a structure standpoint of how the FASB and EITF work together, we talked this morning, thinking about a recommendation to have the SEC and the FASB look at that structure. We missed the quickness that the EITF used to operate under in addressing accounting issues that come up and we'd like to get back to a system where they can be slightly more independent and allow a quicker reaction to one-off accounting issues that come up, and then allow the FASB to address the broader principles and let the EITF handle the more implementation issues and one-off type accounting questions that come up.

Again, we believe that the disclosure and measurement requirements are where we can provide some recommendations and especially as it relates to SB filers and smaller public companies. Our initial thoughts as you think through the -- if you went through a three-tiered
structure, is possibly the SB filers might align themselves
with private companies as it relates to disclosure and
measurement issues. There are, certainly the FASB staff has
allowed certain things to be adopted later or different
measurement criteria, and certain different disclosure
criteria for private companies and should those smaller,
very small public companies take advantage of that, and Jim,
that's where I kind of get to on the size committee, we
probably wouldn't make that recommendation if we were
looking at a two-tiered system. If we were looking at a
three-tiered system I could see us looking along those
lines.

We will bring some recommendations for specific
accounting issues, but it's going to be more of a, you know,
we believe FASB has a full plate the way it is today with
some of the projects that they have in place. I think our
bigger goal here is to recognize a modified approach on a
go-forward basis and then we'll make some recommendations
that the FASB or the SEC look at certain accounting
pronouncements in due time under those same rules, so
hopefully they'll have some relaxation over time and a
different approach to those.

Again, I think overall if I could get two
things into the system to get done, I would like to have
greater auditor involvement in smaller companies, because I
think that's the biggest piece of the pain that companies
feel right now, is, and there's been some guidance just
released from the SEC and the PCAOB that I think is helpful,
but I think even for very small companies there could be a
lot more assistance provided that I don't think jeopardizes
the system and the ability for auditors to issue opinions on
financial statements, and I think we need to get into the
system a simplicity standard that allows companies to be
more consistent, ease of adoption that would make it, again,
would take a lot of pain out of the system and not hurt the
financial reporting that's being done.

MR. WANDER: Steve, did you have a comment?

MR. BOCHNER: Steve Bochner. I was just
curious what you thought about Dave's comment on
materiality. In one of the comment letters we received,
there was a suggestion that materiality be measured on an
annual basis, not a quarterly basis, perhaps for smaller
public companies, sort of getting into this issue of -- and
I'm talking now about for financial statement purposes. I
don't think we proposed to get into the case law definition
of materiality for disclosure purposes, but from a financial
statement, restatement reporting point of view, have you
thought about wading into the materiality issue?
MR. DENNIS: We have not really addressed
materiality as it relates to quarterly versus annual
statements. I know that is an issue and I know that there
are thoughts that I think the SEC is looking at producing a
document that I hope would address that
question. You know, I think as far as eliminating stock
option accounting and determining materiality, you know,
that's a good concept and I understand where it's coming
from. I can name four or five other areas that, well, why
not goodwill, or why not some other non-cash measures and so
I think we have to think through all of that in a
determination of materiality.
I would tell you one of the things we have
talked about materiality as it relates to independent
standards with public accounting firms and their clients.
As it sits right now, there is, materiality is not a
consideration in determining an auditor's independence, and
so I think that's tended to make auditors very conservative,
which puts them in more of an adversarial role with their
public companies. If we could have some kind of materiality
threshold. Right now, if an auditor is judged to be not
independent, it's a very severe penalty for the client,
because potentially their prior three years financial
statements are no longer valid. And a very small
independence violation that may not have an impact on the
company's reporting is potentially just as severe as I own
30 percent of the company's stock, which would actually be
very, very severe.
So one of the things we talked about is whether
we should have some kind of materiality in determining
independence and it all relates around how much auditor
involvement we should have in the financial statements. We
spent a fair amount of time talking about it in our group.
MR. CLOUTIER: Rusty Cloutier. I wasn't going
to ask this question, and then you mentioned goodwill. It
is something that hits home with me and George and I have
discussed it. One of the problems is, is when they change
the rules, you can become very negative and I'll use my
business as an example. The rules have changed in goodwill
in purchase accounting on acquisitions. They have made the
rules that a regional bank can never become a major bank
now. I mean, if you went back and you cost structured
BankAmerica they would be insolvent today, if you put all
the goodwill in, the regulators would rule they couldn't
exist because of all the goodwill they sucked up.

So when you change the rules, there is a major impact to competitive situations. The same thing if FASB goes to mark to market, there are going to be some major changes. You look at it as not one fits all. In my business, I am limited to do a deal that doesn't give me over a billion dollars. Three years ago I could have done a deal that could have gotten me to, you know, be a major player.

So the rules do change. Now, I know FASB's comments, oh, that's not us, that's the federal regulators, but I mean, it's the rules in the game and the games change. I don't think always, as I mentioned in my committee this morning, one of my new directors asked me, "Well, exactly who regulates me?" When I finished giving him a list, he went, "You must be kidding."

There are consequences to all of these things that come about, and goodwill is a good example. Goodwill changed our business dramatically. It is going to stop M&A activity in the banking business very shortly because you can't afford to suck up the goodwill any more. Yet the companies that built themselves, like Wells Fargo, BankAmerica and so forth, they don't have to go back and
restate that, because they would be in a serious bind today,
because they have tons of goodwill on the books. When they
change the rules, there are consequences to that, and maybe
they all thought about it, I don't know, but it did change
the competitive situation drastically in the industry and
maybe it did in some other industries or not.

The other thing I would mention just from a
banking standpoint, and I find we're getting this more and
more. I think accrual is trying to get back at what we go
through. It's amazing in the banking business, we take an
accrued statement, we take it all apart and get back to cash
accounting. As a bank analyst told me one day, you can't
pay a note with an accrued income account.

So we must remember that, too, that at the end
of the day you want to know how much cash is being made.
Often we're having to go through all these rules to figure
if a company can pay us or not. We could have a nice
statement, but if it doesn't have cash flow it could become
a real problem, so that's something else that I would just
encourage you all to think about and continue to give
thought to. George knows I encourage FASB to do that often,
so thank you.

MR. DENNIS: I agree with your -- clearly any
time the rules change it changes the competitive landscape.

I think what you're talking about a lot is not necessarily a
small business issue, but really an issue in the whole
standards setting process. Goodwill is one of my favorite
subjects because I think we spend a lot of time on a
theoretical, I've had this discussion with George also,
theoretical correctness, because it probably is
theoretically a very correct standard. I'm not sure anybody
cares. And I think we need to, it probably has more
relevance to larger companies, but in smaller companies we
need to be cognizant that the users of those financial
statements are people like yourself as a banker, you know,
you tear those financial statements apart. Well, long term,
should the accounting get to where you're already -- you
have them how you want to see them, and I know different
users have different needs.

I don't see us going to a purely cash basis
method of accounting down the road, although cash flow is
obviously real important for any company and that's what
ultimately makes a company survive or not survive. I
believe, Rusty, that we're going to have -- we'll have some
recommendations that the FASB look at standards, goodwill
will certainly be one of those because it's on the top of my
list that we ought to look at, and again, I would go to, I'd
like us to look longer, as we look at standards, that's a
very complicated standard to apply, and it allows a lot of
inconsistency between, and inability to compare companies,
and I would like us to at least be able to make it a simpler
standard to apply so that it is easier for companies to
implement and therefore more consistently applied.

As far as your regulatory issue, I sympathize
with you, because I know your list is a mile long of all the
regulators that you have to deal with, and I would hope that
the FASB and the SEC when they're looking at adopting new
rules takes into account through their testimony and through
their comment letter period the effects on regulatory
issues. A perfect example is the S&L industry and the
changes. In goodwill that happened there. I don't have a
solution for you on that part of it.

MR. SCHLEIN: Leroy, this is Ted Schlein. I
just urge you not to dismiss the whole stock option piece
with other non-cash oriented accounting rules, just because
of what a disproportional disadvantage it could put a small
cap company in on the materiality issues and incremental
costs that could be associated with it, so it was a quick
comment that you made and I just would ask you to spend a
little bit more time thinking about that one in particular.

MR. DENNIS: I think where we struggle with on the stock option issue is, I believe our committee believes its compensation. The rub becomes how do you measure it, and it just so happens that smaller companies tend to use a lot of stock options in their business model. But we do, it took us, literally not very long to say we don't believe we ought to have different recognition criteria mechanisms or accounting standards in small and large companies which kind of gets you on the stock option side of things of FASB, would you like to readdress stock options, again. My sense is they would not. And from a timing standpoint, Ted, by the time we get through our committee with recommendations, it's going to be implemented.

So I'm not sure from a stock option standpoint we're going to have a lot of input in what's already done, but what I would hope is the next time the stock option issue comes along, whether it's stock options or something else, that we could have some input with our recommendations that would allow maybe some measurement or disclosure forgiveness on smaller public companies that allows an ease of implementation, but I believe and I think other people in our committee believe that we should not have just because
you're smaller you should have a different net income reported.

MR. SCHLEIN: I'm not suggesting that. Purely for the measuring materiality was the discussion. Not asking about different net income, I'm not even debating the merits of expensing stock options. That's not the debate. It's centered on one particular point of measuring materiality.

MR. DENNIS: It may be just a one year implementation rule that has to be dealt with as we get this thing adopted.

MR. WANDER: Any other questions? Yes, Al. I'm sorry --

MR. DAVERN: Go ahead, Mark, I'll go after you.

MR. JENSEN: I just had a couple of quick comments. One is, I wanted to speak a little bit about auditor independence and the reliance on auditors. I've been an auditor for a long time, and most of that I've labored in obscurity and I've enjoyed that better than the spotlight that seems to be on us today. I don't think we have to remind registrants that just because things aren't audited doesn't mean they're wrong or the standards have to be lower and I also have to remind them there's a difference
in relying on an auditor for answers versus seeking assistance in solving things. Companies have to acknowledge they do need to be to some extent self sufficient in how they interpret accounting rules. So that leads me to my comment.

I don't believe we're going to see the FASB slow down. Their list of projects is a mile long, and they've got a backlog of projects that people are begging them to look at. It is endless the kinds of things that are in front of them and I'm sure the SEC's list is probably longer than that. The only way I can see us stopping that is to tell everybody you have a quota you get to 20 rules, you're don't for the year and can't do any more. That might be a good idea. I think, certainly, letting small companies implement these rules at a slower pace makes more sense.

Usually the rule is designed for some large situation, anyway, doesn't really have that much impact on smaller companies.

I also, the issue on some of the things we talked about, the FASB is moving to try to align U.S. accounting principles with international accounting standards, that's going to continue. If we don't allow small companies to have some different rules, then they're
going to align themselves with international accounting standards as well. Frankly, as an accountant I think that's not a bad thing. So what I'm saying with all of that, I don't think we're going to see a decline in the amount of rule making. I would like to think that, but I know we won't.

I think the issue is the opinions that come out tend to be arcane, they tend to be written for other accountants, they tend not to have much practical application. There are very few FAQ's that go out, the SEC from time to time puts FAQ's out, but by and large there are very few companies, so you don't see a lot of work being done by the FASB or the SEC in many cases coming out with FAQ's aimed at here's how a smaller companies and transactions more relevant to smaller companies being part of that FAQ's, part of it because they're being written by -- I'm looking for the chairman of BDO's comments tomorrow, because he's got the secret society comment, and I'm anxious to hear that. I'd like the -- I think it's true, by the way, I absolutely think it's true. Some of these accounting rules are written in such a way that the only people who possibly could figure them out are the people that wrote them and they may not be able to figure it out if they had
to apply a real life example to the opinion. I would point to 133 as an example of that.

So, I would just suggest looking at maybe two things. One is encouraging the standard setting bodies to have FAQ's that are directed at smaller issuers. Secondly, I think we've got to start to think about in this country, there's got to be a technology solution to all of this adoption, all of the adoption issues to help companies comply with the accounting rules. I don't know what this is, maybe there's intelligent software we can use or what that all is, but there has got to be something different than what's between my ears to help try to figure these transactions out.

MR. JENSEN: Thank you.

MR. DENNIS: We've had very similar discussions, and I appreciate your comments. I agree with your comments about the FAQ's. I think the technology solution, where we were headed down the road of if we allowed smaller companies to use their auditors more, management still has to take responsibility, they still have to understand it, it's still their numbers, but if we could use the auditors in that transition more, then that would take some of the pain out of the system in the transition to
adopt and I use again the 123 example of when I asked
Patrick, I said, "Do you understand 123?"
He said, "Sure, I understand it all." I'm
probably putting words in his mouth. "But do I understand
123R? No, I don't understand any of it."
If we could get him through that first four to
five years, then does that help with the implementation, you
know, so that's kind of where we were headed as a group,
whether there's a technology solution or not, I don't know.
I think the complicated nature of the
statements -- I jokingly told George that we ought to limit
the FASB to fifteen pages. If they can't write it in
fifteen pages, it's too complicated. That's a joke, but it
has some seriousness to it, in that the standards are so
complicated and they're meant to be what I think is all
encompassing, because we're trying to think of every
possible way someone could violate the rules set in place
and if we go to the SEC's paper on the accounting, maybe we
move to more of a principles base with the EITF dealing with
the implementation issues, but -- I don't have an answer,
but somehow we have to make the system easier for
practitioners and preparers to use and implement and users
to understand, because right now I challenge a lot of people
to understand the disclosures that are in a public company's filings.

Alex?

MR. DAVERN: Thank you, Leroy. I had a comment and a question. The comment is to David. It's Alex Davern here, by the way.

I think when we consider the impact of stock option expensing and other non-cash charges, a system of materiality for 404 reporting purposes I think is something the 404 subcommittee should consider. I do agree with Leroy in terms of pure accounting recognition, I'm not sure it makes sense, but in relation to 404 specifically I think it's an idea that should at least be considered, because it can dramatically change the scope and expense of the process and so we should put that on the table for our discussion.

I also have a question for Gerry. In terms of somebody mentioned, I'm not sure who it was, that, is the SEC looking at a paper on materiality? I hadn't heard that, So I wanted to just pursue that question.

MR. LaPORTE: A paper on -- I'm sorry I didn't understand.

MR. DAVERN: Materiality. One of the speakers mentioned perhaps the SEC was considering publishing a paper
on materiality.

MR. LaPORTE: I think the reference may have been to a paper from the Office of the Chief Accountant, and I'm not sure if that's under consideration or not. I really don't know the answer to your question.

MR. DAVERN: If it is, I think it would be useful for the 404 committee to have some idea of what's going to be in that when it does come out. Thank you.

MR. CONNOLLY: This is Drew Connolly. All kidding aside, Mark, I credit you with this thinking, and it really has helped frame my thinking to be on this committee. The first person I went to speak with after being appointed to this committee, I happened to be in San Jose, I looked up Mark in his office, he was kind enough to spend an hour with me. I emerged shaken, largely because you're talking to a senior partner representing the venture capital industry, one of the largest accounting firms in the country, and I'm down here trying to represent little microcap companies and there's clearly a chasm between the two.

But Mark give me what has framed a lot of my thinking ever since, and I do credit you with that, as opposed to -- and that is when I talked about well, why wouldn't we want to try and make this standard less or why
wouldn't we want to try and find -- he said he was concerned about permanently ghettoizing small issuers. Such that if we were to have three standards, three tiers, we would effectively be creating, the, quote, equivalent of the permanent Pink Sheets and my hope is that we would -- the old days Pink Sheets, because they've clearly improved. 

        My hope is in the exemptive relief we recommend, my sense is every microcap CEO is a midcap CEO waiting to burst out, is that we don't create this tier that by definition is a disincentive to investors to invest or somehow telegraphs that it is a more speculative security, a higher risk just because of its size.

        So I would be prepared to give up some of that ease or simplicity of reporting requirement for, quote, the respectability of being able to attract capital from the big guys. We are supposedly encouraging capital formation, and I'd hate to disincent that.

        MR. BARRY: Can I just make a comment to that?

        I think that part of the recommendation would actually do the opposite, wouldn't ghettoize it. Basically taking the smaller companies and saying, hey, I'm a $25 million market cap company, I don't have the expertise, I believe I should live by the rules of the big guys. We're not saying
different accounting standards, we want the same standards.

We want to go to the auditors and say we want your professional help to make sure we're up to the same level that the big guys are in, so I think it actually professionalizes the smaller companies and puts them on a more level playing field, saying we want the same regulations, we just don't have the resources to go out and get them. PCAOB lighten up, let our auditors playing by the same rules, what's the risk of letting our auditors helping us implement 123R? I don't have the ability to do it myself anyway, I have to go out and spend 50 or $60,000 from a Mercer Consulting or somebody like that. I'd rather have my auditors do it. They're more familiar with it, they need to in the end opine anyway.

It's one of the things, that, I sort of I live in the world and want to get to the next step and I need some help sometimes.

MR. WANDER: Janet?

MS. DOLAN: This is Janet Dolan.

Drew, I think your point is a very good one, which is I think that everyone on our subcommittee has to wrestle with it be ready to address. Are we making recommendations that stigmatize a particular group because
we've somehow lead the public to believe that if you're on one side of the line you're a lesser security for investment or are we creating what we would call sort of "managed implementation differences" so that we can say, the fact that we are treating smaller companies differently in terms of how we choose to implement or the timetable we ask to be implemented or anything else doesn't undermine the security that you should be able to, or the confidence you should have in these companies. It simply acknowledges their size and their resources and other things.

I think all of us when we finally get around to evaluating any of these recommendations we are going to have to take that into consideration saying what message are we sending by the work we are putting forth.

MR. CLOUTIER: One other comment. We made in our committee, and I'd like to make it here for a moment.

In smaller companies you have true independent auditors. Because in my company, in most small companies, we don't pay the auditor enough not to be independent. I mean, they're not going to put their career on the line. The larger the company gets, and the more money they pay, it may be an interesting question of independence, when you are a big hunk of the business as it was with Enron and some of those
I think when you're talking about smaller companies, and Deloitte Touche are my auditors, I think they're very independent, I pay them about $82,000 a year.

MR. JENSEN: Make sure the record shows that.

MR. CLOUTIER: I am sure that for $82,000 a year, no partner is going to put their career on the line. Nothing against my good accounting firm, because they're excellent, but if I was paying 12 million a year in auditing fees, I might get a little more attention. That's all I'm saying, is that you got to remember, small companies have very independent auditors, because we don't have enough to not have totally independent auditors and we don't spend a lot of time looking for loopholes and this is the other thing I wish to point out.

The large companies, when FASB makes a ruling, they automatically sit down for weeks and figure out where the loopholes are, okay? So it's a different playing field, and I think we need to realize that in this room that it is not the same at a $600 million bank as it is at Citicorp at 1.3 trillion. They have a lot more expertise, a lot more people, they maybe figure out a loophole that they can go through the back door that I haven't figured out or
whatever.

So the independence of auditors are very independent in small companies because they'll walk in a minute.

MR. DENNIS: That's a very, very good point and one that I frankly hadn't thought of before, so thanks for bringing that up. That's kind of where we're headed as far as recommendations is that there ought to be more ability for auditors to assist companies like yourself in adopting these standards, because our sense is that doesn't impair independence and maybe the difference is, like you said, a company that pays $10 million in audit fees to its auditor, maybe it's got to live by a separate set of rules than somebody that pays $80,000.

MR. WANDER: I'll tell you a short story about that. I was flying to a board meeting with some clients around the time the Arthur Andersen indictment came down, and being from Chicago, which is Arthur Andersen's home and headquarters, and Chicago was an Arthur Andersen city for a great many years, I said, "Well I'm surprised, because Arthur Andersen audits a number of my clients and they're really very strict. In fact, I think they're stricter than some of the other firms."
And one of the directors said to me, "But Herb, none of your clients are the size of Enron."

That somewhat proves that point. I would like to make one other observation, dealing with the financial statements are the companies and management prepares them and make this observation from an audit committee standpoint. One of the very frustrating things that's going on today is there will be an issue, and management says it should be X and the audit committee says, turns to the independent auditors and says, "Well, do you agree?"

"Well, no, we'd really like to see management fully flesh out that position, and then we'll look at it."

So the company goes back and does a position paper. It's presented to the audit committee. Audit committee says, "It sounds reasonable to us," and the independent auditor says, "Well, I've got to go to headquarters for this one."

So you go to the black box, and the black box comes back and says, "No." You sort of sit back and say well, why did I go through all this trouble, you knew it would be no from day one. Why did I have to go through all this work and everything else, and to that extent they aren't my financial statements.
I must say it's one of the reasons I think that tensions have built up between audit committees and the independent auditors. It's interesting if you look at Sarbanes-Oxley the section mandating independent audit committees specifically says that the audit committee should be the arbitrator and decision maker between management and the outside auditors, which in practice is not true.

MR. DENNIS: Herb, I agree with you, on top of which you'll probably get a qualified opinion on your 404 for having a wrong accounting error under our current system and that's kind of where I'm at. If the auditors can help, for lack of a better word going back to where we were, I'm not sure for smaller public companies that we had a lot of failures that occurred because the auditors assisted in a 123R or assisted in a disclosure matter on a financial statement. Still has to be management's, management still has to take responsibility for it, but I think there's just a different set for companies that are smaller public companies, as opposed to the large cap.

MR. JENSEN: Just a quick comment on this. I think all the accounting firms are in alignment with that recommendation. I don't think any of the accounting firms like where we've been. I think Dan can speak to this, if
he's comfortable, I would encourage him to. I think that
PCAOB has opened this up, accounting firms have loosened up
their ability to work with clients. I think there still is
an issue, and I think it is a good solution now, that
clients have to be actively involved. The point that the
PCAOB has made is, you can't sit back and tell the auditor,
"Okay, just do it to me and tell me what it is." You've got
to work with the issue a little bit.

To your point, I think everybody is frustrated
with national office and I think that speaks to the issue of
arcane accounting principles, that even people around them
all the day can't figure out what's going on.

MR. GOELZER: I think we tried to make as
strong a statement as we could in the May 16th paper about
the fact that it's a desirable thing for clients large or
small to consult with their auditors about difficult
accounting issues and for that matter about internal control
issues, for example, simply asking a question or having a
discussion shouldn't lead to either a material weakness or
to an impairment of independence. That's something we
issued quite recently. Now we'll see how it works out in
practice, but I think we're pretty much on the same wave
length as this discussion.
MR. DENNIS: I think the paper issued by the SEC and the PCAOB is very good and we'll see how that gets fleshed out in this discussion. One of the things we need to think about as a group is, again, if you cross the line on independence, is crossing the line the same for every violation or should we allow some levels of materiality -- maybe materiality is a bad word, but levels of significance in crossing that line on independence, because right now I think we still have the audit firms that want to err on the side of cautiousness as it relates to independence, because the penalties for going over that line are very severe, not only for the audit firm but for the company itself, and again, something I think we want to think about in our group as we continue on here, Herb.

You know, that would go to allowing firms and companies to be more aggressive in adopting what I think the intent of the PCAOB and the SEC is.

MR. WANDER: To Dan's credit, I think Dan has always said that you should be able to consult with your outside accounting firm. I think, unfortunately, not everybody was on board with that and it was very interesting at the round table the SEC held on 404 that the gentleman from GE said, you know, I've got, I don't know, 2,000
accountants working for me, but I need outside help, because
the large firms see different situations with other
companies. So I think there is a great need and I do hope
that the releases that came out on May 16th will go a long
way in solving that problem.

This has been a terrific discussion. Is there
anything else people would like to raise on accounting
standards before we move on to our last subcommittee report?
Steve?

MR. BOCHNER: Thank you, Herb.
I want to start by giving Rusty, who is on my
subcommittee, a piece of advice, which is that it's
dangerous to tell your audit firm that if you paid them $12
million they would pay more attention to you, because I'm
sure Mark was thinking that could be arranged.

MR. JENSEN: That's absolutely true, by the
way.

MR. CONNOLLY: He's Blackberryed that already.

MR. CLOUTIER: As a matter of fact, they
already sent me my increases for next year, they're headed
in that direction.

MR. BOCHNER: I, too, would like to thank the
members of my subcommittee. We've had several meetings and
they approached the issues with sensitivity and intelligence
and I'd like to thank the SEC for the help we've got on our
subcommittee and our Committee Chairs as well. We're the
Corporate Governance and Disclosure Subcommittee and if you
look at the sheer numbers of reforms under Sarbanes-Oxley,
the NASDAQ, the New York Stock Exchange and the SEC changes
in rules, regulations and the statute itself, really, this
is where the most number of changes have occurred.

Having said that, I think it really is the 404
area, which is outside of our purview, that has received the
most attention, because that seems to be where most of the
costs complaints, if you will, are centered.

We have various points of emphasis and focus
that we have narrowed down to and I think it's an ambitious
group of topics that we've been asked to take a look at, and
we were approaching this from the standpoint of where can we
make recommendations to the SEC where we could reduce costs,
while not unduly jeopardizing investor protection, so that
has also been the way we've looked at things, and these are
preliminary.

I want to have all of us keep an open mind.

We're going to hear testimony tomorrow, we're going to have
a couple of other follow-on meetings where we're going to
hear testimony where we're going to continue to get a lot of
good comment letters and responses to questionnaires, so we
look forward to getting those and those do have an impact on
our thinking.

So the first area that we've looked at is all
of the non-404 governance provisions, if you will, and these
would be things like audit committee independence, board
independence, comp and nominating committee independence,
code of ethics, whistleblower provisions, just the range of
items of governance reform that have fallen on public
companies as a result of Sarbanes-Oxley and SEC and SRO rule
making.

I think our initial reaction, based largely on
the comments we've received to date, as I said earlier, this
is not where a lot of the problems seem to be. We're not
hearing a lot of complaints out there yet that people are
having problems complying with code of ethics and audit
committee charter requirements and so on. Having said that,
we do want to take a hard look and receive input on the
independence issue that Dave has commented on.

For example, if you had independent, fully
independent nominating compensation and auditing functions,
would it be okay for smaller public companies to not have
the majority of the board be independent, question. Or is
it that where smaller companies are not having a problem in
this regard?

One of the rationales, perhaps, for considering
that is that smaller public companies have a different
problem set, fewer resources and therefore the directors
that they need to hire may need to have more operational
experience and many of the individuals that they tap for
that operational experience at the director level sometimes
conflict with the independence notions have been developed.
But we want to approach that gingerly we want to get some
feedback and see whether that's a problem.

In the area of the definition of independence,
I think our initial reaction was that these have been pretty
well thought out, although we're open to that as well,
whether the definitions are too restrictive. So we look
forward to getting more comments on that area.

The other area we've looked at is the whole
topic of the acceleration of ’34 Act reports combined with
the new 8-K reporting requirements and we're cognizant of
the fact that public companies in general and smaller public
companies in particular are really getting squeezed by a
combination of having more processes, disclosure controls,
CEO CFO certification processes, internal control issues and so on, while at the same time the amount of disclosure that's required has increased and the time frames are shortened, so that's a big squeeze coming from two different directions, and so we would like to take a look at whether the final phase-down in the accelerated reporting down to 60 and 35 days, 60 days for a 10-K filing and 35 days for a 10-Q filing maybe should be postponed, relaxed, not applied to smaller companies on the theory that perhaps having more time might reduce costs or if it doesn't reduce costs perhaps it would improve disclosure.

We want to get more feedback on that. We have gotten some feedback letters and several of the comments did suggest this and so we're looking to getting more feedback on those topics.

The next area is Regulation S-B and this does get a little bit to the stigma issue that Drew mentioned. S-B filers sometimes feel by identifying themselves as such there's a little bit of a stigma here. We're wondering whether there's a need to have a separate set of regulations. In other words, is one possibility to reduce the amount of overall regulation and maybe help reduce the stigma is maybe not have an S-B, have an S-1, S-3, 10-Q,
10-K for everybody and have a new set of rules under item
S-K, which simply provides whatever relief smaller companies
as we define them get. Is that a good idea or not? We want
to get feedback on that.

Then associated with that, in addition to the
relief that's provided to small business issuers today, and
that 25 million threshold we think is too low, should there
be other types of relief such as the executive compensation
disclosure has gotten so complex, is that degree of
complexity and the cost associated with complying with that
appropriate for a smaller public company or should there be
some different set of provisions that don't require the same
number of accountants and lawyers and internal folks to
comply with that disclosure.

In the SEC's reform proposal, securities reform
proposal, there is some suggestion about broader
incorporation by reference and we think that's a good thing
and we want to look at encouraging a recommendation around
encouraging that where appropriate. For example, even for a
smaller company that might not be able to incorporate by
reference, you know, refer to already filed SEC documents,
should that be considered. In other words, would it reduce
costs, eliminate duplication to allow companies that have
been public for some period of time regardless of size, to be able to reference already filed information rather than having to repeat it in '34 Act filings. So we want to look at that just from a cost of capital raising/cost of compliance, perspective.

Connected to that, we're also intrigued by the direction in the thinking in the securities reform proposal concerning this concept of access, the increasing access among our population to the Internet and documents filed electronically and this idea that maybe it's now time for the presumption to shift and to assume that the U.S. investing public does have access to the Internet and perhaps reduce the amount of paper, which is I think particularly burdensome for smaller public companies, the amount of paper that's produced with respect to not only the capital raising process as suggested in the securities reform proposal, proxy statements and annual reports, many of us get big stacks of this stuff and if you get it electronically you don't need stacks and we'll turn the presumption around, we presume people have access, but if you want a paper copy, there's also a way to get that in a way that isn't overly costly to people who don't have access to the Internet or otherwise want it in paper version.
Will that save money? Is that a good idea? We want to continue to explore that.

And of course these costs are disproportionately higher for smaller public companies which have lower revenue.

The loan prohibition in Sarbanes-Oxley is something we have talked about. We would approach that very gingerly because universally people feel that's a good idea in our subcommittee, but there are some problem areas for issuers out there, just interpretive types of issues, like certain types of cashless exercise mechanisms alone, what about relocation loans? If you're moving from Minnesota to where I live, it's tough to recruit unless you help somebody buy a home, things like that, that, like I said, in our view would be very limited and perhaps conditioned by approval of independent directors.

We talked about materiality, so I won't raise that again.

We also would love to receive input, we're going to do some more thinking about the idea of whether or not there should be a safe harbor for forward-looking information for companies going public. The safe harbor that exists today does not apply to IPOs and as a result you
have companies going public where there's no research
coverage at all, no research done arguably at a time when
the investing public most needs outlook information and is
that a good thing or will that open the floodgates to
companies recklessly providing forecasts out there that
don't have any basis. So we want to take a look at that,
whether the safe harbor should be extended to IPO's. Is
that a good thing? Will it help the capital raising process
or not?

Then we're also anxious to receive other kinds
of input. We're going to continue to explore whether there
are other aspects of '34 Act disclosure, the 8-K
requirements, information in 10-Q's and 10-K's, accounting
requirements and general disclosure requirements that should
be rolled back for smaller public companies, whether what's
there today, sort of a one-size-fits-all in most respects,
really is appropriate or should other types of relief be
extended to smaller public companies.

So that's our agenda.

MR. WANDER: Thanks, Steve, very much. Any
questions or comments? Yes, Kurt.

MR. SCHACHT: Hi, Steve. Kurt Schacht from the
CFA institute.
I was just a little curious about your comment about executive compensation. Most of what we are hearing about executive compensation, we heard from Chairman Donaldson four weeks ago at one of our events, I listened to former Chairman Arthur Levitt just last week saying executive compensation is still sort of the elephant in the living room and there needs to be more transparency and more information associated with executive compensation and how it's calculated and processed.

I think I heard you say that we should look at this in the small company context as being too burdensome and maybe cutting back on that.

MR. BOCHNER: I'm not going to contradict both of those distinguished individuals, but I think that a lot of this was the kind of, you know, corporate jet usage of that kind of thing being disposed and I think a lot of that doesn't exist at the smaller company level. A lot of that is directed at larger company hidden perks, I think that's the kind of thing the comments were focused on. I know you've looked at those tables, but they're very complex today. So I think we're just raising the question whether smaller public companies, that's really, that problem that's been identified really applies to smaller public companies.
or do those smaller public companies really not provide that
many perks because their margins are thin and they don't
have corporate jets and so on.

MR. DENNIS:  And you're not proposing to
eliminate the disclosures completely, just pull out certain
things and make it easier for them to comply.

MR. BOCHNER:  Yes.

MR. WANDER:  Any further questions, comments?

As you can see, there's some overlap among our various
subcommittees, which I don't think can be avoided.  I think
it's actually quite healthy, but we have organized ourselves
on this basis so that we could try and do the maximum job
possible with the resources that are available to us, so
that's why we've organized that way.

Before we move on to the next agenda item, I
wonder if any of the subcommittee chairs or any of the
committee members have any comments or questions to one
another or would like to say something they didn't say in
their remarks?

Yes, Mark.

MR. JENSEN:  Mark Jensen.  One thing I think we
as a group need to think about, I don't want to distract
from the main agenda, but increasingly what we're seeing is
what I'll call the intersection of public companies with private companies and the impact of Sarbanes at the public company level now impacting what private companies need to do, and I'm specifically thinking about partnerships between private companies and public companies where because of internal control requirements of a public company they're looking for comfort around internal control systems in smaller private companies. I think we're quickly seeing in this country that Sarbanes and the governance provisions of Sarbanes are quickly becoming best practices for corporate governance. I think you're going to see a lot of increased litigation coming up in the private company sector because this is the best practice that companies need to aspire to.

I just don't think, for Ted's purpose, I told the venture community I think we're going to see litigation against venture capitalists because some smart plaintiff's layer is going to say this is what best practices are and you're not following it in the private company. This is the way things work in the U.S. When we think about doing things here, this transcends the public environment and it does flows down hill to private companies, so I ask people to keep in the back of their mind when they come up with recommendations.
We're already seeing it. Companies are being acquired, Steve can probably speak to companies being acquired by public companies, require private companies to have almost 404 like systems in place. More and more we're seeing that is becoming shorthand in corporate America for this is how companies do things. I think we do have to, if we're going to make the changes, we have to make some changes now, we need to get this course corrected now.

MR. CLOUTIER: I would like to, if I could, add to Mark's point. As an SEC attorney told me, in my industry, the bank thrift financial industry, what regulator is going to go before Sarbane's Senate committee or Oxley's House committee and say I didn't have these good governance principles in the financial industry. I don't care if your bank did 18 million or 1.3 billion, it is called good governance principles now and it is being enforced right down the line and I think that is very, very important to look at.

And I think, you know, I'm back to a comment Mark made earlier. I certainly hope people would slow down a little bit and study things. I know FASB has this long agenda of things they're dying to do and all of these groups have these agendas. As a person who is an economist by
education, we are in a very good economy right now and
things are very good, but all of these costs come home to
roost when things turn a little sour. And I'm back to my
original statement.

I've never had a company default on me that had
cash. I mean, you know, I'm back to that again, that, you
know, let's when we look at all doing these things, are you
really improving the ability of the company to survive? And
as a person who went through the crisis in Louisiana and
Oklahoma and Texas in the late 1980's and went through some
of that, I can tell you, and i'm not trying to be a
pessimist, but if we get back there again, the kind of costs
we're talking about, is this going to make it better? Did
reserves for loan losses keep the banks strong? I can tell
you very clearly, it didn't.

These are some things we talk ought to
question, all these good governance procedures put on
private companies, is that going to help the country in the
long run?

I'm agreeing with what Mark said. Sometimes we
need to slow down a little bit and say: "What was the
problem?" As I said this morning, Herb, you were in the
meeting, we need to spend a little time on what really
happened with Enron and Worldcom and where the money came from. I'm of the theory follow the money and you know what happened.

We've got a lot of corporate governance things coming up, but we're still not tracing what really happened and if you trace the money I think you know what happened.

That's the only thing. I'm agreeing with Mark, this is happening in my industry big time. The regulators are in the banks like you wouldn't believe.

MR. CONNOLLY: If I may, I would like to agree with my good friend Rusty, who is agreeing with his good friend Mark and we're going to have comity here among the colleagues. Mark obliquely touched on something that I perhaps was going to wait until tomorrow to speak about, but I think it's really critical we recognize that the capital formation aspect of this, one of the four elements in our charter was to encourage capital formation. I'm afraid that in some senses we're being a little too timid. We're acting in the world of, you know, watching out for investor protection.

I assure you, the Enforcement Division Market Regulation and 4200 lawyers at the SEC view that as their mandate, and I know for one that my mandate is to help the
little companies that come to me attract capital so they can
grow, become taxpayers, employers, and somehow find their
way through this mine field of thickets of regulation and
concern that are being put in place allegedly for their
investors to be protected.

So my hope is, as you referenced, here in the
U.S., I am aware and I expect to meet tomorrow afternoon
with the marketing representatives of AIM, the alternative
investment market from London, because they're here in New
York and they're approaching U.S. companies right now to
come off of U.S.-listed exchanges to move overseas, and I am
very concerned that unless we get this right, more of that
will be happening, and that we will in fact be outsourcing
our capital funding opportunities here and encouraging small
business growth.

So I would just request that our friends here
and the folks who may or may not be listening in the broader
world come up with some "art of the possibles" to assist the
companies not only just containing costs, because that's
clearly part of the game, but how do we bring the investors
back? How do we provide the confidence levels and the
enthusiasms to make the United States have their investors
take stock in America, and I'd like to try and figure out
how to do that.

MR. WANDER: Any other --

MR. JAFFEE: I would like to try to make a

comment. I've been sitting here struggling to try to figure

out how to communicate this. Let me take a whack at it.

It seems to me as I've stepped back from all

these problems, and I got my CPA before there was word

processing and we were adding numbers up by hand, okay? So

things were a hell of a lot simpler in 1957. And it seems

to me that much of the problems we've been struggling with

are because we have moved from principle-based accounting to

rule-based accounting. The rules are so complicated and are

so many that a person who wants to find a way around them

does and I won't bother to waste time with all the examples

of how that's happened.

So then our committee is now sitting here

talking about making some, what I consider to be pretty

modest, changes in rules. So we're stuck within the rule

sort of base, and I understand that's what we started out to

do and probably is the only thing we can do, but I'm

wondering if as we give our recommendations if we shouldn't

spend some time in putting together a preamble that is not

so specific rule-based, but deals with principles that have
been talked about in the room here, so that at least we get
on the record for future generations that we're not
satisfied with the principles.

What do I mean by that? First of all, the FASB
thing being so complicated, so difficult, that reasonably
intelligent people are asking for a couple of years so I can
understand implementation. That seems to be crazy. There
ought to be a statement that they ought to come out with
stuff that people can understand.

I think reiterating the idea of the auditors
about being advisers without being compromised for
independence is a principle that ought to be there. I think
there are other things and I'm not smart enough to come up
with them, but I just think the more I think about what
we're doing, make little bitty changes on rules is only part
of the job. That's what I'm trying to communicate.

MR. THYEN: Dick, I think you are absolutely
right. I think a huge cancer is when you become so rules
based that you drive the leadership of a company to do
nothing but focus inside, and to be so concerned about doing
something wrong, and that mind share cost, that opportunity
cost is a huge cancer on successful growth in the
marketplace, which is really the basis for capital formation
and healthy public capital markets. And it is stifling, particularly, you can debate micro, you can debate small, but it is absolutely stifling what we're doing to executive leadership teams of companies that are fighting and struggling to stay focused on their customers, focused on serving their markets in this global competitive world. It's a cancer that's driving us inside. And Rusty, I agree with you. The cash, we've always said, you keep that balance sheet healthy, a local saying is when you go into a famine, a fat man gets skinny, a skinny man dies, and cash is very important. And I think this internal focus is just consuming the cash and the capital and the mind share that is so important for all of our companies to be healthy. Because we're driving inside, the more rules we write, the more we're forced, how do we get around these rules to stay competitive and it's a cancer. We have to get more aggressive.

MR. JAFFEE: I remember when the Enron thing first surfaced in my consciousness and somebody said to me, a special purpose entity, if you have 3 percent outside equity, you don't have to consolidate it. And I said to myself, I don't believe that. That can't be possible. When I went to accounting school, you know, if you owned more
than 50 percent of something you consolidated. I called up
my accounting firm at that time, which was a smaller firm,
we subsequently moved to a bigger one after this, I said
what about this special purpose entity, this 3% thing. I
couldn't get an answer because they didn't have any clients
that dealt with that sort of stuff.

This is the point you were making, Rusty, is
that we smaller people are struggling to deal with a problem
that was not of our own making. There was a few very large
companies that found their way around these very complex
rules. It's just a lot of frustration. I don't know what
the answer is, but it's a lot of frustration.

MR. DAVERN: I'd like to make one comment, Alex
Davern here. I have perhaps a slightly unique background to
bring to bear on this question in that I qualified as a CPA
in the United States when I moved to the States in the early
'90s, but I also qualified as a chartered accountant in
Ireland and the UK in the mid-'80s when I came out of school
in Dublin. When I moved to the States the accounting
standards body in the UK and Ireland was on GAAP standard
was number 22 and the United States was on, I think it was
FAS 109, so I was quite flabbergasted for want of a better
word when I came to the United States and looked at the
rules and the number of rules and the length of the
documents that we were required to apply versus what is
going on in the UK and Ireland, and it was such a gap that
it was hard to credit.

Now, when you come and qualify as a CPA in the
United States you get absolutely no credit for having
qualified anywhere else in the world, so you start from
scratch, given there are so many more rules, I guess that
makes sense. I would echo Dick's comments and, again, this
is probably way outside the purview of this committee and I
don't mean to beat on George here, but it is quite
staggering when we compare the complexity of the accounting
rules here. I don't think anybody would argue that the UK
securities industry is one that people don't have confidence
in. I think the UK securities industry has proved to be
very successful, very robust, very internationally
competitive, and I echo what Drew said, one of the key
messages of the AeA group, is that the burden of regulation,
especially 404, is going to drive certainly foreign
companies to leave the U.S. markets and go elsewhere.

I would urge us to consider this. I want to
make one anecdote, which is probably completely
inappropriate, but I'll make it anyway. The U.S.
Constitution is a pretty simple document, I don't know how many pages are in it exactly, but it's a fairly thin document. The European constitution they tried to get past was about 300 pages long and people didn't understand it, so they didn't vote for it, and when I took a first look at FAS 123R, I nearly fell off my chair because I printed it out on my printer and it's a stack about this thick. So if we can run a country with a constitution of 20 pages, surely we can figure out something a little simpler than that.

MR. BATAVICK: I would like to add something. I take all the comments as very constructive criticism of standard setting in the United States, but if you look at the history of standard setting in the United States, it's that we would love to have started on a principles-based path, but given the environment that we have been in, that we continue to be in, every time we go down the path of trying to set a general principle and general standard, our open due process allows for our constituents to come in and provide a lot of comments. And whether it be the preparer community, whether it be the user community or even the auditor community, it's always, well, what about this, what about that, what about this situation, surely this shouldn't be covered and then what happens is that you start making
exceptions to the general principle that you're trying to accomplish.

If you look at, let's say Statement 133, which is now 875 pages. We started off by saying that derivatives should be measured at fair value, simple. Everybody said, wait a minute, if I'm hedging my oil inventory, you surely don't mean I have to mark that before I sell my inventory are you? Okay, well, what do you want, then? I want cash flow hedge accounting. So once you introduce cash flow hedge accounting -- that's an example.

If you look at Statement 115 where we could have very easily said, if you have a marketable security and the value changes, then mark that through earnings and people said no, we can't do that we're not in a business. So we created three tiers, we had the available for sale, held to maturity. So what I'm saying is that our efforts to try to appease and try to give what we thought constituents wanted has actually ended up creating so many exceptions and so many rules and every time we try to go out with even the simplest of standards somebody says, you know what, we would like to have at least five more implementation examples in the back or we would like to have this paragraph include this or include that.
So perhaps maybe we have tried to incorporate too many of our constituents' views to try not to have any type of unintended consequences of our standards, but by doing that, you're right, we probably have created monsters when it comes to certain standards, so I think the criticism I hear is very constructive.

I think that one of the things both the report of the SEC on Sarbanes-Oxley and most recently yesterday when they released their off balance sheet report they very clearly said we have to move towards more principles-based standards. If we set a principle in Norwalk and if General Electric interprets it one way and is very grounded in how they interpret that, and a smaller public company interprets it that way, and they're all right, what we have to have is a system that allows for both of those transactions being accepted as reported.

And right now I think that you have auditing firms that wouldn't allow that and I think you'd probably have a regulator in Washington that probably wouldn't allow that.

So I think it's going to take not only us to move to more principles-based, but I think it's going to have to have a sea change in the way people think about
things. Of course, the back course of this is also in the backdrop of our litigious society that we have right now.

If you back off, get a little relief on tort and if we could get the preparers and the auditors and the regulators on the same page, then I think we have a very good chance of going to more principles-based.

MR. JENSEN: I want to say something about that. I appreciate your comments. I didn't start in 1977.

MR. JAFFEE: I started with your firm, incidentally.

MR. JENSEN: When I started practicing public accounting, we were on FASB 19, so it's been a few years, although not that many, I'm amazed at that. And typically as a young accountant, when we had an issue with a client, you'd walk in and sit down with a partner, who almost always was male and almost always smoked a cigar, which I hated, and you'd ask the question and they would lean back in their chair and draw upon what I considered to be extreme wisdom and experience, it was probably BS, but he basically worked through the economics of the situation and basically tried to apply common sense to it, and tried to apply the real economics of the situation and let the books and records reflect that. So you had a disparity in practice, because
people saw things differently.

To your point, what changed in the United States, when I started practicing public accounting, if an accounting firm had a lawsuit, it was not discussed openly inside, you were forbidden to talk about it inside the firm. The only people who knew about it were the senior partners. It was considered to be an embarrassment it was assumed somebody made a mistake and that person was going to get punished and we all knew it. What changed in this country is open season on accountants by lawyers. Not to -- it's always my favorite profession and since we had an accountant focus, we can shift it on the lawyers, because we can blame them for everything.

As litigation in the country grew, accounting fees went up to cover that litigation cost, the rules, because accountants were trying to protect themselves had to move away from principle-based, I thought they were principles-based back then, because it was largely figure it out and do what's right.

I think I would agree with your comment. It's outside the purview of this committee, but maybe not. I absolutely believe you're not going to see movement on the part of the accounting firms backing away from the kind of
low threshold on materiality, the kind of judgments that's being applied without some kind of meaningful tort reform.

There's a group of us in the room, there's a few of us in the room that every day bet our houses about five hundred times a day that somebody in our firm got it right and if they didn't we've got enough capital to cover what the damage is going to be.

MR. DENNIS: Mark, I want to add a couple of things. I heard your CEO talk one time and I think his comment was if your client lost a half a percent on its market cap and they blamed the auditors you're out of business.

In support of FASB staff, the comment I would make is I don't think there's very many pronouncements that were issued that are not in response to something. To some extent we're our own worst enemy here. We wouldn't have issued FIN 46, which is a fairly simple standard, it says don't do what Enron did. But it's I don't know how many hundreds of pages long trying to figure out, because what everyone wants to do is Wall Street comes in and says, well, what about this, here's a way I can do this, so the FASB staff says here's a way I'm going to stop you from doing this.
To some extent we're our own worst enemy with trying to develop ways around the rules, and you can't write enough rules to do that.

I would love to get to principles-based standards. I think we have to have management, Wall Street and the accountants all with the guts to stand up and say we're going to be a principles-based economy.

And I wonder as I hear some of the comments here, if we've tried to write rules to protect the 1 percent of the companies that are dishonest at the expense of punishing the 99 percent that are honest people and just trying to do good for the shareholders.

MR. CONNOLLY: Hear, hear.

MR. DENNIS: The problem is the 1 percent that are dishonest are probably extremely dishonest, but I'm not sure if anything we've done with SOX or anything else is going to stop that, because if they're dishonest, they'll figure out a way around it and hopefully the lawyers and Wall Street will try not to associate with those people. A lot of theory, and I don't know if it means anything, Herb, but it's a couple of comments I heard from here.

MR. CLOUTIER: Herb, let me mention a couple of things just from my experience, put things a little bit in
perspective, to go back to Chicago, 1989, Continental Illinois Bank. Continental Illinois today would be a community bank. The country has changed dramatically in fifteen years, dramatically, and I think we need to realize that. When we talk about, well, we don't want different standards from small companies and large companies. You're not talking about a little large company now, you're talking about humongous companies. Companies that can write a check for $2 billion for the involvement in Enron and not even take a blip in their stock price, just walk right by it and say yeah, we were engaged, okay?

Two billion fifteen years ago would have shut down any company in this country, so it is really, really different.

As someone told me the other day, try to think of an industry that is not totally becoming consolidated and we're talking about the smallest part of the industry down here at the 500 million market cap and under. I mean, I'm sure Deloitte has more than 500 million in capital, so those can go bankrupt every day, it wouldn't bother them. We have changed, again, so dramatically in this country by consolidation that it is a different game. I mean, if you want to talk about retail, you want to talk about food
services, you want to talk about banking, you want to talk

about oil, you want to talk about agriculture, any of those,

it has become a totally consolidated industry with fewer and

fewer players and the small people are just trying to make

their way into it.

I'm not sure there's not already a difference

perceived in the market between the large and the small and

maybe we're kidding ourselves by saying that we put S-B or

something on them or we have different accounting standards

the market is going to treat them differently. Everybody

understands that the bank regulators recently came out with

something that I think was very good, that is complex and

non-complex banks. I'm a non-complex bank. In other words,

I'm in the banking business, I'm not in options trading,

derivatives and all this other stuff and they regulate you
different. I think that's important for us to think about.

It's a different country than it was fifteen years ago.

MR. SCHLEIN: In an effort to bring this back
to the SOX conversation, the macroeconomics, I'm sure are

not lost on anybody, and just doing the math as a cost

benefit analysis for the country, or for the economy, 8,000

public companies, average of $2 million per public company,

put a 20X multiple on it. I can't do the math in my head,
but I'm sure it's in excess of a trillion dollars in market value. That's what you're trading off for some of these new reforms or these new rules.

Is it worth it, is it not worth it? That's to me the macroeconomic view of this.

MR. THYEN: I think one other thing, building on that, Ted, what we're trading off is any smaller company, building off of Rusty's comment of consolidation, is that all smaller companies compete on skill, they don't compete on scale, and the very large companies compete on scale, they leverage the entire supply chain. Maybe you call it complex, non-complex and the regulations, the rules, when they're specific to the general, one Enron, therefore, apply it to all, kills skill. It kills innovation, it kills flexibility and it stifles all of the things that grow smaller public companies. It takes away all of the skill that we compete on in the marketplace.

MR. WANDER: And you don't have the cushion of the $2 billion settlement. It's interesting. A friend of mine said "It's unbelievable that someone could pay $2 billion on the JP Morgan Chase settlement and nothing happens, nobody goes crazy or the stock doesn't drop or anything else."
I think this discussion has been healthy. I don't want to really cut it off, we don't get a chance to get together that often, but everybody's views I think are extremely valuable.

Jan?

MS. DOLAN: I wanted to follow up on Ted's comment. I thought what we heard in the last 45 minutes, the level of frustration you hear, I think you can magnify that by thinking of the frustration of everyone we represent, the public companies. We're not going to change our litigious society overnight, but we can say what can we do, working on Ted's comment. We can first of all put the cost value relationship in front of people and come up with practical pragmatic recommendations that address it.

We can't make the SEC or PCAOB or anybody else do it, but at least we can do our job, which is to say here's some very practical proposals that match what should be regulated with the scale and value that it creates for small companies.

So I just think we've got to stay very focused on not getting too far afield in terms of all the reasons why it wouldn't work and stay very focused on what we really can do to make a difference and it can make a difference if
we stay very focused on what can we do to try to make this a much more rational reaction rather than the overreaction one-size-fits-all that we've been living with for about two years.

MR. CONNOLLY: My final remark, I know it's a little hard to believe --

MR. WANDER: It's not, I'm sure.

MR. CONNOLLY: You're probably right.

Drew Connolly. The one part, speaking to that, Janet, to the art of the possible, what's feasible, without having to be scope-free, because frankly we managed to get it on the initial agenda, there is a whole lot of pushback, firstly, I guess to make this fully encompassed. We obviously need to thank Gerry and Allen, the folks within the Small Business and Corporate Finance Division of the Commission, but there's a whole lot of pushback in a couple of the other divisions to the issues of small business, and I don't know how many of us have interacted with them or have concerned ourselves with them, but I'll take Market Regulation, because Enforcement is for another day, right?

Market Regulation, as I understand it, has a real problem with small business generally and with a very specific issue fundamentally and that issue is of finders,
and just a quick anecdote. Last week I was in Bellevue, Washington, a client of mine is headquartered there. We were standing around, a securities attorney was sitting around talking, saying, "You know what, my client is the largest Mercedes-Benz dealer in town. His customers come to him all the time and say, 'We got some money, you got any great companies we can put it in here?'"

The Mercedes dealer knows three or four companies that need capital. He wants to figure out how to get paid and he can't get paid under the current scenario without becoming a either a registered advisor or a broker-dealer. I've spoken to our observer, who is the securities regulator for the State of Nebraska, as to what would satisfy on an unofficial basis the state regulator's concerns about finders. I have not had access to the Market Regulation people as to what would satisfy their concerns, but it seems to me that a very simple registration; name, address, phone number, Social Security, education, some of the issues that go into a CRD filing with the Securities and Exchange Commission so they know who is doing what to whom and more importantly if you're a little company looking for money you have a central database of people who professionally raise money might not meet that test and help
in the capital formation issue.

MR. WANDER: Gerry.

MR. LaPORTE: I don't know if you realize this,
but the American Bar Association appointed a task force on
finders about three or four years ago and they did issue
their report last week. I'm sure the SEC staff is going to
take a careful look at that report, so you may see some
traction on that issue from the SEC in the future. I'm not
promising anything, but one of the outstanding issues was
what position is the American Bar Association was going to
take.

MR. CONNOLLY: I hate to ask this in the middle
of a law school but are the lawyers on our side?

MR. WANDER: I've read the report. Yes, I
think so. It's for, what you say, sort of a mini-
registration so you have jurisdiction over people, hopefully
you clean up the marketplace. You probably can get it on
the web page, the Business Law section of the American Bar
Association, and if you can't, let me know and I'll get you
a copy of it. It's actually got some very prominent names
that have signed it. I mean, people you would think would
not be involved in this very small mini-cap finders arena.

MR. CLOUTIER: Herb, Rusty Cloutier. Just one
comment back to Janet's comment, I wanted to mention, I think it's very important to write a preamble, like James said. I think that is critical. We've got to get that message out.

Let me say one thing, having represented small companies the last five years, and the job I had on the board of independent community bankers, believe me, they spend a lot of time making sure that small bankers have a difficult life. When we put out there changes for the small companies, they're going to show up immediately saying no, no, no, no, no, we don't want them to have any advantages.

I'll give you one example, this is almost laughable, but with the Federal Reserve Bank, we just have got them and the OCC to agree to raise CRA from 250 million to a billion dollars. The financial services round table representing the fifteen largest bankers in the country, smallest member is $600 billion, said that it would be competitors to them and they're not sure they could stay in business if the small banks were given this opportunity. So that's why you have to have a preamble, because the large companies are going to show up and say you shouldn't cut them anything. They work very hard, don't think they don't spend a lot of time on these rules thinking how much of a
problem it is to them and how much of a problem it is their competitor. If you don't think those two thousand people they have are not working every day, they are.

So, I think a preamble is very important to set the tone before you come with the changes, because I think otherwise there's going to be a lot of comments that the changes aren't needed.

MR. WANDER: Jim and I, we call that the me-too complex. It exists, there's no question about it.

There's a famous Alan Jackson song about the big guy drove the little guy out of business. In fact, that's in large part what's happening in the country as evidenced by the consolidation and so we are the finger in the dike, hopefully we'll be even more important.

Again, I don't want to cut off comments. Are there any others? If not, why don't we go on?

The next item on the agenda is the discussion of factual input, and first hearings. We are having hearings tomorrow morning. We would propose to have hearings in Chicago and San Francisco. It really would be helpful if each of you would let us know, Jim and I and Gerry, what subjects you would like to have covered, where we need further input, who would be a good witness, because
this is a great opportunity for us to get sort of one-on-one
with many of these people, ask them questions and have
presentations by them. I have talked, for example, to the
person who designs the Russell Indexes who will be in
Chicago, he wasn't available to come here, and what their
thought process is and how they do that, because very
interestingly, one of the initial ideas we had on the size
was picking something like the Russell 2000 and now I
understand Russell is going to have a new index that's
coming out June 23rd which is really, they were going to
call it the microcap but it's actually the bottom thousand
of the Russell 2000 and the next one thousand companies
which I think they say represents about 8 percent of the
market cap.

So think of people like that that you'd like to
come in and provide information for us.

The second area is questionnaires. I know
Steve has sent one in, of questions that he would like to
publish that we can ask for public comment on, and I would
hope that each of the subcommittees could get us a list of
questions, because time is fleeting, really, we'd like to
get them out. They have to be in a certain format under the
SEC rules, but I think if you get us the questions we'll be
able to format them so that it's appropriate.

The next is the SEC Office of Economic

Analysis, and Cindy has been here this morning, she's from

that office, she's been extremely helpful, and Alex must
talk to you every day, I guess, asking for additional

information, Cindy Alexander, so we have good support there

and each of the subcommittees or any particular member if

you think that there is something that she could be helpful

with, let us know.

And we're also going to try to get some

additional help from the SEC's Office of Risk Assessment,
because I think they are looking at how should the

Commission view companies, how should it be proactive ahead

of the next bubble that breaks and what are the risk

profiles that we may need more regulation or at least more
disclosure, et cetera, so we think that would be helpful.

If there are any other areas that you'd like us
to look into, let me know and in fact it was interesting,

Drew, that you mentioned AIM. I have a set up an

appointment to conference them by telephone to see what

other countries are doing about alternative trading markets.

MR. CONNOLLY: One of your witnesses tomorrow,

John O'Shea, was kind enough to allow me to come down to his
office to meet with the AIM folks, but he is, without
telegraphing his story, is enroute over to Dubai. He is a
member of multiple exchanges and has offices in various
parts of the world, but there is about to be a fairly
vibrant Middle Eastern exchange in Dubai and I think there's
a tier being created over there for their smaller type
companies.

MR. WANDER: We actually saw in one of the
magazines, San Paolo is setting up a small cap trading desk,
in effect, a trading floor. The information we have on AIM
is very sketchy, at least going through sort of the
Google-type searches and other information, but we're
looking into that as well. So time is somewhat limited and
our resources are somewhat limited, but if you give us some
ideas on other areas to look at, we will try and find
experts or get information.

Any comments?

MS. DOLAN: Herb, I just would say I think the
answer we got on whether there is some definitive work being
done on the SEC materiality was incomplete. That's a fairly
significant issue, so I would say that you or Jim, something
is owed in answer to that shortly, so we're not off in one
direction if we find out there's actually some substantive
work going on in another.

MR. DENNIS: There is. I am fairly confident there is something going on at the SEC, in I'm not sure which division, on materiality, but I'm not sure they know the timetable as to when, and I think, I thought that was common knowledge, quite frankly. I can follow up Herb if you want.

MR. WANDER: I think, isn't it the Chief Accountant's office?

MR. JENSEN: It's Alan Beller, and Alan announced at our last meeting that they're working on that, so it's public knowledge.

MR. DENNIS: I think their big issue is transition, as I understand it, as to how to deal with transitional issues.

MR. JENSEN: Having said that, I thought to myself "good." The last time the SEC added rules on independence, we added 30 percent to the audit fees. Just to kind of help the SEC out. We've been nice to them this afternoon.

MR. WANDER: That is one of the problems. Speaking for lawyers, we're one of the worst offenders as well, because we say we want bright lines. When a regulator
draws bright lines, they are always in the wrong place.

Right?

MR. JENSEN: They're always up here, never down here.

MR. WANDER: So we want all these rules and we want all this direction. I would, somebody asked this morning, actually, I'm going to send out the Trumbell report which is the English version of COSO. It's 12 pages, it's not AS2. Somebody said, "What's the liability? Is the liability greater under those circumstances than it is if you had a 380-page document?" And I personally think that liability would be less, but because you're less apt to trip over things than you are if you have all these rules.

And really what Mark said earlier about, when he first came into the business, well, what are the economics of the situation and you should account for it that way.

So in any event, that's something that we all bring on ourselves, I guess, the Chinese proverb.

I put on the agenda, "reaffirm or revise committee agenda," and I only did that so that if any of the comment letters moved us to such an extent that we should revise our agenda, I thought it would be appropriate to at
least explore that issue. I'll be blunt to say I don't think -- I think the comment letters were very helpful, but I don't think they have shown us some different direction other than probably don't be too ambitious, do a good job on the areas you're dealing with.

Is there any thought about revising or adding to or subtracting from our agenda?

MR. DENNIS: Herb, on the accounting principles area, one of the things we've talked about is emphasize importance of cash in smaller companies. Okay, it's important. I'm not sure what else we should say as far as work that we need to do. It's important, we all recognize it's important. I'm not sure we're apt to take off into a different measurement criteria for cash in the accounting world, so I'm not sure what we're going to do around that item, other than to say yes, it's important.

MR. WANDER: Didn't Don Nicholaisen suggest that he liked the other cash flow statement than the one that's generally used? I'm not smart enough to go any further than that.

MR. BATAVICK: I think the direct method as opposed to the indirect method? He may have said that on occasion and that is on our agenda in phase B of our
financial performance project that we have with the IASB, so

I would say it's probably within the year that that issue

will be addressed and so far the initial reaction is

pushback.

MR. WANDER: That's interesting. That's

interesting. But the analysts, too, I mean, if you looked

at some of these companies when the bubble burst, if you

sort of said what was their reported net income, and then

you looked to see what they paid out in dividend and then

you'd see what was my increase in net worth, it didn't jive.

Something was missing, and it was cash from there.

But very few analysts pointed that out, in my

view. In any event, I'm going to go on.

Discussion of our timetable. Jim and I

actually discussed this with our leaders at the SEC staff,

whether, frankly, the change of leadership at the SEC might

suggest to us that we either speed up or slow down our

timetable, and I think our conclusion, which we submit to

all of you, is that we stay on course with our timetable

that's out, to have our job done in thirteen months, but I

did want you to know that we looked at it and if any of you

have any comments or suggestions, we're obviously open to

them.
The next item is next steps, planning for the August meeting. We will try and have the August meeting out very soon, the agenda, et cetera. List of witnesses, please get those to us as quickly as possible. It will probably be another day and a half meeting. One of the reasons I sort of scheduled it in Chicago at that time is it's at the conclusion of the American Bar Association annual meeting which will be in Chicago, and as a result we probably will have a number of people we can get to stay over who I think would be very helpful as witnesses in our hearings. So that's one of the reasons we chose Chicago.

Hopefully, the weather will be great, Dave, right? Not too hot, not too cold.

MR. DENNIS: Herb, we were wondering if the Cubs were in town.

MR. WANDER: Well, since I'm a White Sox fan--

MR. THYEN: Those tickets are half price, right?

MR. WANDER: The White Sox are in town that previous weekend. I don't think the Cubs are. We have the best record in baseball, but no attendance.

Are there any other items to be brought before the Committee? If not, we would adjourn, we can adjourn,
but I would like to make one comment.

Having spent so far all day today and our previous meeting with all of you, I am enormously impressed by the dedication and skill and experience that you all brought to the table here, and can't thank you enough for really volunteering to be on this committee. I think our discussion that we just had shows you the importance of this for essentially the country, the economy, and I must tell, say to each of you that you're just doing a superb job, at least I thank you and I'm sure Jim does, too.

MR. THYEN: I would like to echo that. I said earlier in our opening comments that we are diverse in our experience, our background and our points of view, and yet the caring, committed way in which we're approaching this professionally and to keep the problems on the center of the table and focus on the problem rather than on our differences I think is very, very commendable.

Thank you for your time.

MR. WANDER: Hearing nothing else, we're adjourned. Thanks.

(Time noted: 3:53 p.m.)
CERTIFICATION

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

Herbert S. Wander
Committee Co-Chair

September 12, 2005

Exhibit A: List of Members of the Public Who Provided Written Statements and Presentations

Jun. 17, 2005 Professor William J. Carney; see also slide presentation
Jun. 17, 2005 Edward S. Knight, Executive Vice President and General Counsel, The Nasdaq Stock Market, Inc.
Jun. 16, 2005 Murray S. Cohen, CEO, Epolin
Jun. 16, 2005 John P. O'Shea, President, Westminster Securities Corp
Jun. 16, 2005 David L. Cox, Chairman, President and CEO, Emclaire Financial Corp., Farmers National Bank
Jun. 15, 2005 Opening Statement of David N. Feldman, Managing Partner, Feldman Weinstein LLP
Jun. 14, 2005 Gayle Essary, Managing Director, Investrend Research and CEO, Investrend Communications, Inc.
Jun. 13, 2005 Andrea Psoras, Principal, Strategic Advisory; Member, New York Society of Security Analysts
Jun. 12, 2005 Samuel J. Yake, Paoli, Pennsylvania
Jun. 10, 2005 R. Cromweli Coulson, Chief Executive Officer, Pink Sheets
Jun. 08, 2005 William (Bill) A. Loving, Jr., Executive Vice President and Chief Executive Officer of Pendleton County Bank on behalf of the Independent Community Bankers of America
Jun. 08, 2005 Philip V. Oppenheimer, Oppenheimer & Close, Inc.
Jun. 08, 2005 Steve Nagel, President, Kolorfusion International, Inc.
Jun. 08, 2005 Karl Kirwan
Jun. 08, 2005 Victoria Duff, CEO, Bold Ventures Group
Jun. 07, 2005 Michael Ramos, CPA
Jun. 07, 2005 Fred P. Barwick, Barbara Blackford, Linda K. Wachtel, Subcommittee on Smaller Public
Jun. 06, 2005 Richard D. Brounstein, Chairman of the Small Public Company Task Force, Financial Executives International and Member of the SEC Advisory Committee on Smaller Public Companies


Jun. 01, 2005 Deloitte & Touche LLP


May 31, 2005 Robert J. Kueppers, Chair, Center for Public Company Audit Firms

May 31, 2005 Ernst & Young LLP

May 31, 2005 Charles W. Barkley, Attorney at Law, Charlotte, North Carolina

May 31, 2005 Ronald J. Simpson, Chief Financial Officer, Minefinders Corporation Ltd.

May 31, 2005 Debra Fiakas, CFA, Managing Director, Crystal Equity Research, New York, New York


May 31, 2005 Joel Jameson, President, Silicon Economics, Inc., Cupertino, California

May 31, 2005 BDO Seidman, LLP

May 31, 2005 KPMG LLP

May 30, 2005 Michael T. Williams, Esq., Williams Law Group, P.A., Tampa, FL

May 30, 2005 David N. Feldman, Managing Partner, Feldman Weinstein LLP

May 26, 2005 Peter Chepucavage

May 26, 2005 Steven J. Sharp

May 26, 2005 Phillips W. Smith, Ph.D., Paradise Valley, Arizona

May 24, 2005 Kathryn Burns, Vice President and Director of Finance, Monroe Bank

May 24, 2005 John B. Williamson, III, Chairman, President and CEO of RGC Resources, Inc.: RGCO; Director and Audit Committee Chairman of Optical Cable Corporation: OCCF; Director and Audit Committee Chairman of Botetourt Bankshares Inc.: BORT.OB


May 24, 2005 Brad Smith, President, WBS&A, Ltd.

May 23, 2005 Scott Shaw

May 17, 2005 James A. Brodie, Managing Director, Carr Securities

May 11, 2005 Frederick D. Lipman, Blank Rome LLP, Philadelphia, Pennsylvania