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RECORD OF PROCEEDINGS OF SEC ADVISORY COMMITTEE  
ON SMALLER PUBLIC COMPANIES

Tuesday, 12 April 2005

9:30 a.m.

SEC Headquarters, 450 Fifth Street, N.W.  
William O. Douglas Room, Suite 1C30  
Washington, D.C.

1 The following individuals were present in person:

2 Committee Members:

3 Patrick C. Barry

4 Steven E. Bochner

5 Richard D. Brounstein

6 Pastora San Juan Cafferty

7 C.R. "Rusty" Cloutier

8 James A. "Drew" Connolly III

9 E. David Coolidge, III

10 Alex Davern

11 Joseph "Leroy" Dennis

12 Janet Dolan

13 Richard M. Jaffee

14 Mark Jensen

15 Deborah D. Lambert

16 Richard M. Leisner

17 Robert E. Robotti

18 Scott R. Royster

19 Kurt Schacht

20 Ted Schlein

21 James C. Thyen

22 John B. Veihmeyer

23 Herbert S. Wander

24

25

1 Committee Observers:

2 George J. Batavick

3 Daniel L. Goelzer

4 Jack E. Herstein

5 SEC Commissioners:

6 Chairman William H. Donaldson

7 Commissioner Harvey J. Goldschmid

8 SEC Staff:

9 Anthony G. Barone

10 Alan L. Beller

11 Mark W. Green

12 William A. Hines

13 Gerald J. Laporte

14 Donald T. Nicolaisen

15 Kevin M. O'Neill

16 Chester Spatt

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## 1 P R O C E E D I N G S

2 CHAIRMAN DONALDSON: Why don't we get going if we  
3 can. Good morning to everyone. Once again, welcome to the  
4 SEC. I am pleased to be here for the first meeting of the  
5 Advisory Committee. I want to say again, as I said last  
6 night, to those of you that were able to be there how much we  
7 appreciate what you are doing here. This is a real service  
8 for the SEC. And I want to particularly thank Jim and Herb  
9 for their leadership, which has already been evidenced by the  
10 caliber of people sitting around this table.

11 As everybody knows, this work is very important to  
12 the country and to the SEC, and I might add to me personally.  
13 Having had a bit of involvement in helping to start and run a  
14 small business, I know what it is like to run a small  
15 business. And I know how difficult it is to get something to  
16 get something going. And I know how difficult a regulatory  
17 overlay can be in terms of damping down potentially  
18 entrepreneurship. So I think that it just goes without  
19 saying how important entrepreneurship and small business is  
20 to this country.

21 I have spoken on numerous occasions about the  
22 reforms that the Commission has passed in the wake of  
23 Sarbanes-Oxley. Last month, I took pen in hand and wrote a  
24 brief commentary that appeared in The Wall Street Journal  
25 entitled, "We have been Listening," and that is what we are

1 doing. This is a part of this listening process.

2           The SEC established the committee to examine the  
3 impact of the Sarbanes-Oxley Act and other aspects of the  
4 federal securities laws on smaller public companies. This  
5 committee will conduct its work with a view to protecting  
6 investors, considering whether are the costs imposed by the  
7 current regulatory system for small companies are  
8 proportionate to the benefits, and identifying the methods of  
9 minimizing costs and maximizing benefits. I know that you  
10 will present us at some point here, upon the completion of  
11 your work, some thoughtful recommendations, and we really  
12 look forward to receiving them.

13           Now I will ask all of you to stand if you will and  
14 raise your right hand and I will administer the oath. As a  
15 member of the Securities and Exchange Commission's Advisory  
16 Committee on Smaller Public Companies, do you promise to  
17 assist the Commission in evaluating the securities regulatory  
18 system of issuer disclosure, financial reporting, internal  
19 controls, and offering exemptions for smaller public  
20 companies;

21           Two, conduct the work of the committee and make  
22 recommendations on the current regulatory system that you  
23 believe will protect investors, ensure a regulatory system  
24 that minimizes cost, maximizes benefits, and facilitates  
25 capital formation by smaller companies, and faithfully

1 execute all duties of a member of the Advisory Committee  
2 necessary and appropriate to meeting the goals and objectives  
3 of the committee charter.

4 If so, will you please say I do.

5 [Members respond affirmatively.]

6 Thank you, please sit down.

7 I am going to turn the podium over to Alan Beller.

8 MR. BELLER: Thank you, Chairman Donaldson. I will  
9 be very brief. I mostly want to echo what the Chairman has  
10 already said this morning, both as to the Commission's and  
11 the Division of Corporation Finance's gratitude to all of you  
12 for having accepted this charge to be either a member, or in  
13 the case of three of you, an official observer to this  
14 committee. And, secondly, to underscore the importance that  
15 we believe that this committee's work holds for us.

16 Obviously, most of the headlines about  
17 Sarbanes-Oxley and its impact on smaller public companies in  
18 recent weeks and months have focused on the internal control  
19 provisions of Section 404 of that Act. That is certainly one  
20 of the things the committee is going to, as we understand,  
21 undertake to look at. But, as the chairman has mentioned and  
22 as I have mentioned on other occasions, the charge of this  
23 committee is broader than that. I think we are hopeful that  
24 this committee will bring a focus to all of the provisions of  
25 that Act and their impact on smaller public companies. And,

1 frankly, to go beyond Sarbanes-Oxley. It has been many, many  
2 years, it has been since the early 90's since our disclosure  
3 regime for "small businesses" has been looked at. And there  
4 are a number of governance issues that relate to smaller  
5 public companies that we believe merit your attention. And  
6 certainly there have been almost every year, or I guess every  
7 year at the forum that we run for small business, the issue  
8 of capital formation comes up as a major issue. That is  
9 certainly something that we are hopeful that this committee  
10 will also take a look at.

11           As we will discuss later in the day, there are a  
12 number of parts of the Commission and the staff,  
13 particularly, but not limited to, the Division of Corporation  
14 Finance where we hope to provide resources to this committee,  
15 and we hope to support the work of this committee. But  
16 having gotten a group as expert and experienced and talented  
17 as this around the table, we are really looking forward to  
18 receiving your recommendations. And I believe I speak for  
19 the Commission, I know I speak for the Commission in that it  
20 is also eager to receive your recommendations as to the  
21 matters that we should be looking at when it comes to our  
22 rules and other things.

23           With that, I am going to turn matters over to our  
24 two co-chairs, whom I would again echo the chairman and  
25 especially thank for having agreed to take on this

1 assignment.

2 James Thyen and Herbert Wander, gentlemen, the  
3 floor is yours and the meeting is yours.

4 Thank you very much.

5 MR. THYEN: Thank you, Alan. I am Jim Thyen and  
6 good morning and welcome. I have a few opening comments and  
7 then I will turn the meeting over to Herb and he will conduct  
8 the meeting. I am not going to repeat what Alan and Chairman  
9 Donaldson said to us as we are generally in alignment with  
10 those comments. But this is the beginning of a new day. We  
11 have come together here, many of us meeting for the first  
12 time, and we are a diversified group, diversified in thought  
13 and experience and ability and in background. And we  
14 represent a broad class, a broad cross-section of  
15 constituencies of small public companies. And of course we  
16 are sponsored by the Commission to advise them on this  
17 matters.

18 Our goal will be to bring meaningful  
19 recommendations of change in administration and regulation,  
20 doing so in a way that the SEC willingly wants to accept our  
21 ideas. The law and its administration has at times forced  
22 cost choices and mind share shift on small public companies.  
23 That often is out of balance and not proportional. For some  
24 small public companies, it drives opportunity costs and is at  
25 odds with the global competitive world in which we compete.

1 For many companies, that cost is very much at conflict and  
2 increases the competitiveness of low-cost venues around the  
3 world. So the SEC clearly recognizes that. It recognized  
4 that fact and that is why we are chartered as an advisory  
5 committee.

6 And so we seek over the next 13 months to advise  
7 the SEC on how to gain greater balance and proportionality in  
8 applying the law. We do that recognizing that we represent  
9 and speak on the behalf of small public companies. That is a  
10 privilege of access to the public capital markets and it  
11 brings with it a higher standard of performance and  
12 compliance.

13 So we look forward to the journey and the beginning  
14 of a new day. Thank you for accepting the challenge of  
15 serving on this committee and serving with Herb and myself.

16 MR. WANDER: Thank you, Chairman Donaldson, Alan,  
17 and Jim. My remarks are going to start with how we are going  
18 to operate and progress through the end of our tenure, which  
19 hopefully will be within a year from now.

20 Jim and I are going to share chairing meetings.  
21 This meeting I am going to chair and Jim will chair other  
22 meetings. And we hope to follow parliamentary procedures but  
23 on hopefully an informal basis.

24 A number of people have asked me about our  
25 recommendations, how will they be presented, in what form, in

1 what substance, and then what happens to them. There are a  
2 number of levels to look at this particular issue. First,  
3 there is the statutory level, primarily Sarbanes-Oxley, and  
4 the 33 Act and the 34 Act, all administered by the SEC.  
5 Congress adopts those statutes and in order to change the  
6 statutes, we would have to go make recommendations through  
7 the SEC to change the statutory wording or sections of either  
8 of those Acts or any other Acts. In forecasting where we are  
9 going, I doubt very much whether we will be suggesting  
10 legislative changes because those are very difficult to get  
11 through Congress. It takes a long time. And I think there  
12 are other more appropriate avenues for us to follow than  
13 trying to have legislation changed.

14           So I am turning now to the SEC's ability to make  
15 rules and regulations. The SEC has very extensive authority  
16 to adopt rules and regulations to implement the congressional  
17 statutes. And this is the area that is most fruitful I think  
18 for our endeavors, is to at the end of the day make  
19 recommendations to the SEC on how to change rules, revise  
20 them, and hopefully in all cases improve those rules.

21           Now the SEC in adopting rules and regulations has  
22 to act under the Administrative Procedure Act and so what we  
23 will do is hopefully make recommendations in writing to the  
24 SEC. The Commissioners will then consider those. And if  
25 they are in agreement, they will then propose rule changes.

1 Those rule changes will be proposed publicly and then there  
2 will be a comment period required under the Administrative  
3 Procedure Act where the public will have an opportunity to  
4 comment on those changes. And then the SEC will consider  
5 those comments and a host of other factors in determining  
6 whether to adopt the rules that originally were recommended  
7 by us. And, as I said, this is where I think our major focus  
8 will be.

9           The SEC also has more informal processes. They can  
10 issue FAQ's, Frequently Asked Questions, that give the public  
11 and companies and investors and attorneys and accountants the  
12 ability to understand how to interpret and apply the  
13 regulations. The SEC may also issue what they call Concept  
14 Releases. There is a concept out there and they would like  
15 to flesh it out further without adopting it or proposing a  
16 specific rule. And that might be another avenue for us to  
17 pursue.

18           It will take some time so that those of us who are  
19 anxious to see changes made, hopefully we can make some  
20 recommendations before the end of our tenure so that the  
21 Commission can act on those and consider them earlier than  
22 others. But even if the SEC does that, they have a process  
23 to go through and it will take some time to do that.

24           Now what about the substance of our  
25 recommendations? I don't think any of us have any definitive

1 preconceived notions about what our recommendations will be,  
2 but I suspect that if all of our recommendations are quickly  
3 adopted by the SEC, we have probably not been bold enough.  
4 And I think what we are here about is to really un-peel the  
5 onion and to try and get at the guts of what is investor  
6 protection and then try and improve it in light of what the  
7 economy needs in terms of promotion of smaller business,  
8 entrepreneurship, particularly in the global economy.

9           It also may take more time for some of our  
10 recommendations to come to fruition. It may be they are a  
11 little premature and so maybe it will be a couple of years  
12 from now or even 10 years from now when the wisdom of our  
13 recommendations are finally seen. But I hope that with our  
14 foresight and our ability to gather facts and bring to bear  
15 all of our experiences, our recommendations will be keenly  
16 accepted by the Commission and then by the public and then  
17 adopted. And those that may take a little longer, we will  
18 have to keep our eyes on that ball and make sure eventually  
19 they are adopted.

20           That is enough of the introductory remarks. Just a  
21 housekeeping item and that is when you speak, would you  
22 please announce your name because we are web casting this and  
23 it is very difficult for anyone listening to this to try and  
24 figure out who is speaking. So please announce your name.

25           And now I think we can begin to discuss the agenda.

1 The first item on our agenda, formal item, is approval of the  
2 by-laws. And those have been submitted to you in your  
3 pre-meeting packages. Is there any discussion or a motion to  
4 approve the by-laws as submitted?

5 MR. CONNOLLY: James Connolly. I move that we  
6 adopt the by-laws as submitted.

7 MR. WANDER: Is there a second?

8 MR. DENNIS: Leroy Dennis, I second it.

9 MR. WANDER: Thank you. And now is there any  
10 discussion before we hold a vote on the by-laws? Hearing  
11 none, all in favor say aye, please?

12 [Chorus of ayes.]

13 MR. WANDER: Opposed or abstentions. Okay. Thank  
14 you very much. We got our first item of business done very  
15 quickly, and we are off to a great start.

16 Now as sort of a housekeeping matter, I think all  
17 of the committee members have been told that there is a  
18 federal statute dealing with advisory committees and that  
19 much of what we do, including our meetings, have to be in the  
20 public forum, which is fine and we are very compatible with  
21 that. In addition, taking advantage of web pages, I think a  
22 lot of what we do will be very transparent because the  
23 committee's agendas, major papers, et cetera, plus all public  
24 comments that we receive will be hopefully put on the web  
25 page. And I would like Jerry Laporte to just take a minute or

1 two to describe our web page so all of you are aware of sort  
2 of the fish bowl that we are going to be living in.

3 MR. LAPORTE: Thank you, Herb. All of you in the  
4 materials that were passed out this morning, you got a sample  
5 of a recent printout of what this advisory committee's web  
6 page actually contains. We have been updating as we go  
7 along. We intend to keep on updating it as the life of the  
8 advisory committee proceeds on. We are anxious to have any  
9 suggestions. I know there are several people on this  
10 advisory committee who are much more technically competent  
11 than I am and perhaps not all the SEC staff. But we are  
12 interested in getting some suggestions. If anybody has any  
13 specific suggestions on how we can improve it, that is fine.  
14 Right now, we have releases on there, various Commission  
15 releases that have been issued, published for the advisory  
16 committee. We have materials for this meeting. I think we  
17 received three written statements for this meeting. They  
18 should all be up. And as we attract additional written  
19 statements for different meetings, they will all be up on the  
20 web page. And if anybody has any questions, I can try to  
21 answer them today or you can give me a call or give one of  
22 the staff members a call at the Office of Small Business  
23 Policy. I think you have our numbers in the contact list  
24 that was sent out, and we will be glad to try to help you.

25 MR. WANDER: Are there any questions for Jerry? I

1 think in working other commissions, particularly for the  
2 American Bar Association, I have found these web pages to be  
3 invaluable because you have at your desk access to almost all  
4 of the papers and submissions that come in and almost on an  
5 instantaneous basis. And so it is very helpful. And as the  
6 day goes along, you will see that we do want to get not only  
7 input from the committee's members but also from the public.  
8 And we are going to encourage that so that all of our work,  
9 all of the ideas that are out there that we may not be aware  
10 of can be presented to us.

11 So having no questions on the web page, I would  
12 like to move on to the next item on the agenda, which is a  
13 substantive item, and that is a discussion of the committee  
14 agenda, which at the conclusion of today's meeting under item  
15 VIII on the agenda, we would like to have formal approval.  
16 Now what the agenda is is a sort of roadmap that Jim and I  
17 and the staff members from the SEC helped prepare and it is  
18 not written in concrete. It is written as a sort of prod  
19 everybody to think of additional items that they would like  
20 to have or to say this is too ambitious, perhaps we should  
21 eliminate some of these items on the agenda.

22 What will happen with the summary agenda, if  
23 adopted by the committee, is it will be published by the SEC  
24 for comment, and we will ask members of the public to comment  
25 on whether there should be items put on the list, items

1 deleted from the list, areas where improvement is needed. We  
2 are going to ask for specific recommendations. It is very  
3 good to complain but complain with a purpose in mind of  
4 telling us how to improve things. And also whether the cost  
5 benefit analysis is working properly as Jim mentioned in his  
6 opening remarks. So this is going to be the first piece of  
7 information that we send out to the public. This is our  
8 agenda, tell us whether you the public, whether investors,  
9 small business people, accountants, lawyers, et cetera,  
10 anyone who is interested, believe it is the right agenda and  
11 we will ask for comments I believe in 30 days once it is  
12 published.

13           So with that as an introduction, the floor is open  
14 for comments, suggestions, revisions, and improvements to the  
15 agenda. We couldn't have been that perfect.

16           MR. CONNOLLY: Mr. Chairman, James Connolly. Under  
17 capital formations, number seven, I would propose that we add  
18 an examination of the role of finders from a registration  
19 standpoint. I know there is a lot of discussion to  
20 institutionalize finders and the role of finders and the  
21 registration requirements of finders such that the SEC's  
22 mandate for investor protection is met and that professional  
23 capital finders have a central point of both registry and  
24 uniform registration without the onerous burden as is  
25 currently determined with a full broker-dealer registration.

1           MR. WANDER: Are there any further comments on  
2 adding the subject of finders? For those of you who aren't  
3 quite familiar with this, this has been a subject, a repeated  
4 subject I should say, of the SEC's Small Business Forums,  
5 which in the background and briefing materials we sent out to  
6 you we have the last three year's recommendations. That has  
7 been one of the recommendations that has appeared. And the  
8 purpose of that is essentially to smaller businesses  
9 frequently raise money on a more informal basis. They don't  
10 have the benefit of the large investment banking firms. And  
11 so the question is whether the person who provides access to  
12 capital should be registered or whether they are operating  
13 within the law. I think that is the sort of scope of what  
14 the suggestion is.

15           Any further comments on that? I suspect what we  
16 ought to do is we will include it and then at the end of the  
17 day when we approve this, that will be one of the items  
18 included unless somebody has any disagreement with that.

19           MR. CONNOLLY: Thank you, Mr. Chairman.

20           MR. WANDER: Did I see a hand somewhere? Yes,  
21 Mark.

22           MR. JENSEN: This is Mark Jensen. There have been  
23 a number of letters and some even this morning. I am  
24 wondering if the content of those letters, if anybody has had  
25 a chance yet to reconcile comments from the public with the

1 agenda and add appropriately the things that have been raised  
2 in those letters? I haven't looked at everything that is in  
3 front of me.

4 MR. WANDER: I did read the two letters that came  
5 in last week, and I think they are covered. I haven't read  
6 this morning's. Maybe we could do that.

7 MR. JENSEN: Maybe we could do that before we  
8 finalize the agenda.

9 MR. WANDER: To finalize the agenda, that is a good  
10 idea.

11 MR. JENSEN: And make sure because I think if the  
12 public has taken time to react to it, we should certainly had  
13 their suggestions.

14 MR. WANDER: Any other additions, corrections?  
15 Yes, Dick?

16 MR. JAFFEE: Dick Jaffee. I don't know whether  
17 this is a matter for the agenda or for the mission of the  
18 commission. I had been under the understanding initially  
19 that our work was going to be limited to the effect of  
20 Sarbanes-Oxley. This morning I understand more, that it is  
21 broader in scope. Is that a matter for discussion on our  
22 agenda before we even get started or has that been accepted  
23 as part of the mission of the commission from the beginning?

24 MR. WANDER: I think if you read the SEC's  
25 announcement of the establishment of the advisory committee

1 and our charter, which is on file, it is broader than  
2 Sarbanes-Oxley. For example, in this whole capital formation  
3 area, there are a number of issues that have been around, as  
4 Alan said, for 10, 12, I guess 13 years, since the early  
5 1990's. It is a project that Congress is very interested in  
6 is promoting smaller businesses. And so I would think that  
7 based on our charter and the direction from the Commission,  
8 we should continue to include topics other than just  
9 Sarbanes-Oxley unless somebody has some objection to that.

10 MR. JAFFEE: Well, I think we should too but I am a  
11 little bit worried that if we make it so broad that our  
12 efforts are going to get diluted and we are going to have  
13 trouble within the time frame, focusing down and getting  
14 something accomplished. That is a comment.

15 MR. WANDER: That actually is a very good comment  
16 because when we prepared the agenda, we probably put on more  
17 than we can actually accomplish. That is one of the reasons  
18 we established subcommittees, so that we can leverage the  
19 talent that is on the committee in various areas so not all  
20 of us have to attack every area. And I would hope that the  
21 subcommittee chairs would come back to us during the whole  
22 course of the deliberations and not only feel free to add new  
23 topics that come up but also to say we just can't get this  
24 done in time and do a good job on that. And then part of our  
25 final report may be an agenda for future issues that we

1 weren't able to cover. But this is a good point, Dick.

2 Any others?

3 MR. SCHLEIN: Mr. Chairman, Ted Schlein. I think  
4 possibly under Section 6, accounting principles, I would like  
5 to propose that we maybe discuss at some point the effect of  
6 the impending stock option expensing might have as a burden,  
7 an undue burden on the small cap companies and highlight that  
8 as something that we should at least discuss and evaluate.

9 MR. WANDER: Any other comments on that particular  
10 topic?

11 MR. DAVERN: Alex Davern. I would agree that that  
12 is a topic that should be considered.

13 MR. WANDER: Don Nicolaisen will be here later so  
14 we will make sure we tell him that after he has worked so  
15 hard in putting out his release last week on that issue.

16 Any other comments? And if no objections, we will  
17 include that in the final vote under item six. Thanks, Ted.  
18 Janet?

19 MS. DOLAN: Chairman Wander, this is Janet Dolan.  
20 As the chairperson of the subcommittee on Section 404, I am  
21 not recommending any additions to the outline at this time,  
22 but I would just follow up on your previous comment, which is  
23 to say that I think it is quite obvious from reading the  
24 agenda that the categories under Section 404 are probably  
25 more generic than the other categories, they are very broad.

1 And we will do our best as soon as we can to help define some  
2 of those and break them down into more granular subsections  
3 so it is easier for the public to direct their comments on  
4 specific activities that are under our scope. So we will do  
5 that.

6 MR. WANDER: Thank you very much. John, did I see  
7 you had your hand up?

8 MR. VEIHMEYER: Just one comment on the list.

9 MR. WANDER: Your name?

10 MR. VEIHMEYER: John Veihmeyer. One comment on the  
11 list, recommendation in item 62 under accounting principles  
12 where the agenda indicates that one of our objectives is to  
13 identify priority accounting principles where modifications  
14 may be considered, which I would think would include the  
15 consideration of stock option accounting. And I am wondering  
16 whether or not we want to identify in our agenda only one  
17 specific accounting principle when there may be a number of  
18 principles that would fall into that category that we would  
19 address. So I am perfectly in support and in agreement with  
20 evaluating stock option accounting if part of the charter. I  
21 am wondering about whether we ought in the charter -- or the  
22 agenda, identify one of what may be several or many  
23 principles that we would want to look at. That is my only  
24 comment on the last recommendation.

25 MR. WANDER: Well, I think there was a Texas and a

1 West Coast sort of focus on the expensing and it is such a  
2 big item. Perhaps I will play and lawyer and what we could  
3 do is put "including but not limited to."

4 MR. VEIHMEYER: Agreed.

5 MR. WANDER: I think unfortunately the water may be  
6 under the dam but it may not be under the dam for smaller  
7 businesses and there may be ways of cushioning the blow,  
8 particularly in terms of cash is king or queen. And so the  
9 use of non-cash compensation can help a great many small  
10 companies.

11 These ideas have all been very good. Are there any  
12 others? Yes, Steve?

13 MR. BOCHNER: Mr. Chairman, Steve Bochner. This  
14 doesn't fit neatly into any of the categories but it is  
15 taking longer for companies to get public. And so I am  
16 wondering whether one of the issues we ought to look at is  
17 the exemptive scheme for employee benefit plan issuances  
18 under Rule 701 and whether the thresholds still work given  
19 the longer period of time it takes for companies to be in a  
20 position and to have the infrastructure to go public. So it  
21 is definitely not capital formation, it doesn't fit under  
22 that.

23 MR. WANDER: It might fit under your committee  
24 actually, governance and disclosure. I don't know. I don't  
25 know. You are the third person who has mentioned that by the

1 way in the last 24 hours. Those of you who know about the  
2 issue it is whether exemptions for essentially private  
3 companies to offer stock-based compensation should be  
4 enlarged. It is an item maybe we should -- does anybody else  
5 have any comments on that particular item?

6 MR. LEISNER: Herb, Richie Leisner, there is the  
7 Section 12 ramifications of those situations we ran into sort  
8 at the end of the tech bubble, if you have enough option  
9 holders you could wind up inadvertently being required or  
10 possibly being required to register under Section 12 as a  
11 public company.

12 MR. WANDER: That again, let me elaborate just  
13 slightly on that. Unfortunately, the securities laws use  
14 registration in two areas, one is under the 33 Act when you  
15 are selling securities to the public, you have to register  
16 it. In the 34 Act, if your company is large enough and has  
17 more than 500 shareholders, you have to "register" again and  
18 that is not to register a stock sale but to register the  
19 company. And that is what Richie is talking about, that if  
20 you have a lot of option holders, you can become a public  
21 company and there are some large companies that were public  
22 in that way. I think the United Parcel Post was one of them  
23 before they actually went public. We should figure a way to  
24 fit that in, and we will do that and I will let you know how  
25 we fit it in before we vote on it if that is all right with

1 everyone.

2 Are there any other suggestions, comments,  
3 improvements?

4 MR. DAVERN: Mr. Chairman, it is Alex Davern here.  
5 I had one that I would like to consider under Section 2. It  
6 is very focused obviously on the execution of 404 and 05 and  
7 what worked well and what didn't work well and so on. I  
8 think it might also be appropriate to consider at the  
9 subcommittee level the effectiveness of internal controls as  
10 a fraud prevention mechanism at small public companies,  
11 specifically fraud perpetrated by executives and senior  
12 officers and evaluate how effective it is in principle at  
13 preventing those frauds. That may require some consideration  
14 of the post mortems of actual frauds that have had happened  
15 and so on that we might want to consider.

16 MR. WANDER: Any comments on that? In fact, if you  
17 look in your briefing book, we sent out for the public that  
18 is here, we sent out a briefing book with articles and  
19 statutes and other information. One of the articles in the  
20 briefing book is by the AICPA, which is a recent paper that  
21 they have published. It is entitled, "The Achilles Heel of  
22 Internal Accounting." And it is management override. So,  
23 yes.

24 MR. DAVERN: Sorry, that is exactly what I was  
25 referring to and there are other similar data out there which

1 I think seriously should be considered by the committee in  
2 terms of the fundamental effectiveness at the small company  
3 level of internal controls.

4 MR. WANDER: So is there any comment on that? If  
5 not, we will add that, Alex.

6 MR. DAVERN: Thank you.

7 MR. WANDER: Thank you. Any other comments?

8 MR. CONNOLLY: Mr. Chairman, James Connolly. Once  
9 again, broadly under item 7, capital formation, as there is  
10 often necessary tension between the Securities and Exchange  
11 Commission, the National Association of Securities Dealers,  
12 and the North American Securities Administrators Association,  
13 and much of that impacts the process of essentially accessing  
14 capital and going public as there are rightly currently I  
15 believe multiple different, whether they are merit review  
16 states or whether they are exemption states, and I think of  
17 504 specifically, which is the \$1 million raise, I would like  
18 to think that we could do certainly not an exhaustive but I  
19 expect that we will be receiving comments throughout the  
20 period from both the NASD and from NASAA, that we take a look  
21 at the interplay between the Securities and Exchange  
22 Commission, NASAA, and the NASD because, as you well are  
23 aware, any company looking to file to go public has to file a  
24 15C211 on the smaller cap side. And that is examined,  
25 submitted by a broker-dealer for no compensation, and then it

1 is examined by the NASD examiners, often with multiple  
2 comments. And that information from the 15C211 is not  
3 materially available to the public, both prospectively and  
4 archivally. So perhaps there is a reason for us to look at  
5 how these different organizations work, interplay of the  
6 access to capital side of things.

7 MR. WANDER: Any further comment on that  
8 suggestion? It is the interplay of state regulation, and we  
9 have Jack here, who is an observer from NASAA, and the SROs,  
10 which means self-regulatory organizations, such as NASDAQ.  
11 And I think that could be added to the interplay of the state  
12 regulation and SRO regulation under item number seven.

13 MR. CONNOLLY: Thank you, Mr. Chairman.

14 MR. CLOUTIER: Mr. Chairman, Rusty Cloutier. One  
15 thing, I don't know exactly where it fits, but definitely  
16 under the accounting rules in other places, a lot of  
17 corporations have different regulators. As an example, I am  
18 in the banking business. We have the Federal Reserve, the  
19 OCC, they have their own rules and regulations and sometimes  
20 they co-exist with the SEC, sometimes they do not. And  
21 sometimes it puts companies in a very difficult situation.  
22 There are other laws, such as that requires banks to use GAAP  
23 accounting automatically, it does not give any discretion and  
24 sometimes changes. And I think maybe in some industries we  
25 need to look at that carefully. And I think the banks

1 themselves are going to be looked at in the future as we hear  
2 about this to be utilized somewhat as agency to work with  
3 some groups, as we were discussing last night at dinner, to  
4 make sure that GAAP accounting is followed by companies and  
5 whatever. So I think that too needs to be looked at very  
6 carefully.

7           Just one slight example, being in the banking  
8 business, I have signed a call report every quarter for 36  
9 years. And the OCC has plenty ability to put me in jail if I  
10 file a false statement. So attestation to sign at the end of  
11 the quarter for the SEC is no big deal for me because the OCC  
12 comes in every year and verifies every figure. So I think  
13 this is something we need to look at and other issues like  
14 Drew was talking about, other regulatory agencies and the  
15 people that are involved, how does this affect us going  
16 forward. I don't know exactly where it fits in but it is  
17 something I think we need to look at.

18           MR. WANDER: Well, as a first stab at that, perhaps  
19 we could say something like overlay of other regulatory  
20 accounting requirements, regulatory accounting and  
21 substantive requirements, at least put it in the accounting  
22 principles for the time being. But it is not just banks but  
23 it is other regulated industries that do have -- particularly  
24 in the insurance area that do have an overlay of additional  
25 requirements. That is a good suggestion.

1 MR. DENNIS: Mr. Chairman?

2 MR. WANDER: Yes.

3 MR. DENNIS: Leroy Dennis. Under item five, I  
4 would like to suggest we have got in there the special  
5 exchange Forms 10-K, 10-QSBs. I would like us to look at the  
6 benefits of a full 10-Q filing for small business filers. I  
7 would include in that whether or not there needs to be  
8 auditor involvement. For example, should we go to a six  
9 month full filing and then some kind of limited disclosure on  
10 a quarterly basis and would that still give the investors  
11 what they need for a smaller business and yet take some cost  
12 burden off of those full 10-Q filings.

13 MR. WANDER: Any comments on that suggestion?

14 MR. CONNOLLY: Do you mean on a voluntary basis or  
15 a submission to the Commission as opposed to a voluntary  
16 audit?

17 MR. DENNIS: I guess I haven't thought that far  
18 through the process. The only thing I would make sure is  
19 that if this was allowed in a company, to make sure that  
20 there is adequate disclosure to the shareholders of what  
21 information they are and are not getting.

22 MR. CONNOLLY: I will ask because the fellow who  
23 was the president of the pink sheets, Carma Colson, has a  
24 very, very strong position on compelling some level of  
25 disclosure even for his non-reporting and I very much support

1 that.

2 MR. DENNIS: My initial thought is that there would  
3 not be no disclosure, that maybe you would need some kind of  
4 revenue information, something like that. I haven't thought  
5 it all the way through.

6 MR. CONNOLLY: Ownership.

7 MR. DENNIS: Ownership, maybe some kind of brief  
8 MD&A disclosure or something like that. But is a full  
9 certified or reviewed 10-Q required and does it add investor  
10 benefit for a company of say \$50 million, \$25 million in  
11 revenue.

12 MR. WANDER: Any other questions or comments about  
13 that suggestion? In fact, fact one of Alan Beller's  
14 predecessors, the late Linda Quinn, had suggested going to a  
15 semi-annual report for all companies. My own personal view  
16 is I don't think that is possible in today's world but for  
17 smaller businesses, there may be some merit in examining what  
18 they should be doing on a quarterly basis is what you are  
19 saying, isn't it?

20 MR. DENNIS: Yes.

21 MR. ROBOTTI: Mr. Chairman, Bob Robotti. I don't  
22 see why we don't put it on the agenda. Of course I fall into  
23 the camp that says the other thing since I am an investor in  
24 companies that have \$50 million market caps, I do find 10Q's  
25 to be an extremely valuable piece of information and their

1 management discussion analysis, the results, those are all  
2 important things that I don't see how you have a market that  
3 kind of properly adjusts the pricing and identifies things if  
4 you don't have kind of quarterly reporting. So there is no  
5 reason not to put it on the agenda. I fall into the camp  
6 that says as a user of those statements, I find them  
7 extremely useful. And if I did not have 10Q's, that would  
8 impair our ability to understand companies and developments  
9 and companies and therefore impact pricing I do think.

10 MR. WANDER: You can see the diversity of our  
11 committee. It depends whether you are buying or selling,  
12 right?

13 MR. DENNIS: And the only question I would ask is  
14 whether or not you need the full information of the 10Q for  
15 say a \$50 million and the expense and cost of gathering that  
16 information. Could you make appropriate investor decisions  
17 with less information? That would be what I would ask you to  
18 consider.

19 MR. WANDER: But we should add it and we will put  
20 consider the benefits of. And we will see where we come out  
21 at the end of the day. Yes, Steve?

22 MR. BOCHNER: Just a comment on that. Steve  
23 Bochner. A related question is perhaps we can take a look at  
24 is that the way the CEO/CFO certifications are set up is that  
25 you really can't file unless you can certify you fully comply

1 with the form. And a lot of companies are having trouble  
2 filing because of whistle blower issues or 404 related  
3 issues. And so I think one of the things we should look at  
4 is whether it is a good thing to have companies file even  
5 though for example the review might not be completed or  
6 whether it is better to wait until you get it all done even  
7 if that means that you are not going to be able to get the Q  
8 on file for a couple of quarters. So I think it is related  
9 to that comment. Is the fully comply requirement good for  
10 investors?

11 MR. ROBOTTI: Bob Robotti again. That is a great  
12 point because we have over the last number of months been  
13 confronted with a number of situations where companies have  
14 not been fully compliant, therefore have not reported results  
15 and potentially have gone for months at a time without really  
16 disclosing financial data. So that you really do have a void  
17 that really starts to open up. Here they are telling you we  
18 are not sure about internal controls, we are not sure about  
19 what the right numbers might be, and haven't even disclosed  
20 what they think the preliminary numbers might be. So  
21 therefore that really starts to create a lot of uncertainty  
22 in the marketplace, the failure to give any disclosure.

23 MR. WANDER: I think our friends from the SEC would  
24 say you should do as much disclosure as possible under those  
25 circumstances but it is a good subject now with more avenues

1 of question open for people, we should look at that.

2 MR. ROBOTTI: Of course, that is not necessarily a  
3 small business issue, right. There are very significant,  
4 very large companies today that are not publicly filing on a  
5 timely basis and have not disclosed financial information.

6 MR. WANDER: I think we will find in a great many  
7 situations what we are going to be examining applies across  
8 the board, not just to smaller businesses. I think the  
9 proportionality does but I think in terms of some of the  
10 regulations, as you just said, that could apply to any  
11 company.

12 MR. BATAVICK: Mr. Chairman, George Batavick. I  
13 notice that in Section 6, accounting principles, it would  
14 appear to me that the focus is on existing accounting  
15 standards. I would suggest also that we consider in the  
16 future accounting standards, effective dates and transition,  
17 and whether or not they should be different for small  
18 business filers versus the larger public companies. As  
19 everyone is probably aware, a lot of times at FASB, when we  
20 do issue accounting standards we give extended effective  
21 dates to private companies. We also give them maybe  
22 transition differences that are not afforded public  
23 companies. So perhaps that should also be on our list for  
24 considering for future standards.

25 MR. WANDER: Any comments on that?

1           MR. ROBOTTI: I think that is an excellent  
2 suggestion.

3           MR. WANDER: Very good. I find myself spending  
4 more time trying to figure out the transition rules than the  
5 rules themselves sometimes. Okay.

6           MR. SCHLEIN: Mr. Chairman, Ted Schlein. There is  
7 an environmental factor that I don't know where it exactly  
8 fits but I think it is important to make sure that it gets  
9 discussed and figure out the impact, which has to do with a  
10 lot of the small cap companies inability to get Big Four  
11 accounting attention. So it is not necessarily a particular  
12 auditor issue, it is the environment that has been created  
13 where companies have been dropped from Big Four accounting  
14 attention, what positive or negative impact that might have,  
15 I won't draw a conclusion yet. And also environmentally  
16 something that we see a lot is the changing the dynamic  
17 between the auditor and the company where it used to be one  
18 of a collegial business partnership. I would characterize it  
19 more as adversarial or at least potentially controversial.  
20 And, as I said, it is an environmental dynamic that I think  
21 is evolving and is starting to exist. And I am not exactly  
22 sure where it gets handled as part of the agenda.

23           MR. WANDER: Well, are there any other comments on  
24 that?

25           MR. ROYSTER: Mr. Chairman, this is Scott Royster.

1 I agree strongly with the point that was made. I think that  
2 there may even need to be an entire section devoted to a  
3 conversation about the role of the outside audit firms  
4 relative to all the legislation that has been passed because  
5 the power dynamic has shifted dramatically. And really the  
6 outside audit firms are the gatekeepers of a lot of the  
7 legislation that has been passed. And I think there needs to  
8 be a much broader conversation about the role of the outside  
9 audit firm as it relates particularly to smaller companies.  
10 And so I would wholeheartedly support the notion that there  
11 perhaps even be another section devoted to that topic.

12 MR. WANDER: Did I see Janet?

13 MS. DOLAN: This is Janet Dolan. Again as the  
14 chair of the internal control, I was going to offer to take  
15 at least the resource implication because I think that is one  
16 of the cost constraint factors into ours. But if the  
17 decision of the body is to have a separate section and then  
18 put some of these issues there, that would be fine as well.

19 MR. WANDER: We could add I think something to item  
20 six, current industry environment and discuss the  
21 concentration of the Big Four, the smaller firms, and the  
22 gatekeeper issue that Scott has mentioned.

23 MR. DENNIS: Mr. Chairman, this is Leroy Dennis. I  
24 understand the SEC and the PCOAB are in the process of a  
25 joint statement on guidance to auditors relating to this

1 topic? I don't know if anyone from the SEC can comment on  
2 that?

3 MR. WANDER: Well, Dan Goelzer.

4 MR. GOELZER: Of course as I think most of you  
5 know, there is a roundtable tomorrow on 404 reporting. And I  
6 think many people feel that at least part of the adversary,  
7 arms-length relationship between clients and their auditors  
8 comes out of some of the things related to 404 reporting. So  
9 I think it is at least a subject that will be discussed at  
10 the roundtable tomorrow and possibly one of the things that  
11 either the Commission or the board or both of us will follow  
12 up on from the roundtable.

13 MR. WANDER: Alan?

14 MR. BELLER: I would just add I agree with Dan. I  
15 think it is virtually certain that the issue of the  
16 relationship between auditors and preparers will be something  
17 that is discussed in the roundtable tomorrow. I took Scott  
18 Royster's point frankly as being a little broader than just  
19 the issue of whether that relationship has become excessively  
20 arms-length. As I say, I thought that was a broader point  
21 but I leave that to the committee.

22 MR. ROYSTER: Mr. Chairman, Scott Royster again.  
23 It is a broader point because I think we need to look at  
24 things such as cost of outside audit firms. The  
25 supply/demand imbalance that exists given that there are only

1 four firms and there are thousands of public filers,  
2 obviously there are lots of other outside audit firms but  
3 most public companies at least I think have the intention of  
4 defaulting to one of the Big Four but it is becoming more and  
5 more difficult for smaller companies to do so. And then of  
6 course the various power dynamic issues that I think have  
7 really strained relationships. We have historically at my  
8 company looked to our outside audit firm as professionals we  
9 could go to for advice and counsel. And, quite frankly, that  
10 relationship no longer exists for the most part. We have had  
11 to bring in a lot of internal resources. And that is fine.  
12 If we have to basically hire up to help us understand certain  
13 matters, we will do that. But with respect to smaller  
14 companies, I think that is a fairly significant economic  
15 challenge in the short term.

16 MR. WANDER: I think the note keeper will make that  
17 broader Alan. This has been a very helpful, thoughtful set  
18 of comments. Yes, Dick?

19 MR. JAFFEE: Dick Jaffee. Herb, can I just make  
20 one more comment on this whole subject of the auditors and so  
21 forth. It seems to me that another thing that has happened  
22 besides the lack of collegial consultation is that the whole  
23 issue of materiality in the audits has been put into some  
24 question as it related particularly to the 404 thing where  
25 all these new definitions of material deficiency and all

1 these sorts of things have come up, and if we are going to  
2 look at that whole relationship, I don't know what we can do  
3 about it but I think it is a reality that the things that we  
4 used to rely on in terms of size of problem and material  
5 impact on the result have been all sort of thrown up for  
6 question. And I don't know where they come down right at the  
7 moment frankly.

8 MR. WANDER: I am just wondering the whole question  
9 of materiality, you could write a book about, which is not to  
10 say we shouldn't discuss it.

11 MR. DAVERN: Mr. Chairman, Alex Davern. I think it  
12 would perhaps make sense if I could make a suggestion that we  
13 add that to the 404 or the internal control subcommittee as I  
14 think that is an absolutely key element we have to address to  
15 try to make sense of the cost benefit relationship for  
16 smaller companies. And I would like to also add on to what  
17 Scott said earlier on that I think we should somewhere in the  
18 committee's work specifically address the issue of the point  
19 of confusion that exists out there in the market today around  
20 what auditors can and cannot give advice on. And that we get  
21 a practical, sensible common sense end result to how auditors  
22 and their clients can engage in meaningful business  
23 conversations because there certainly seems to be different  
24 interpretations between what the public comments of the SEC  
25 and the PCOB have been and what the practice is on the ground

1 in dealing with public company auditors.

2 MR. WANDER: Janet, we are loading you up.

3 MR. DENNIS: I was going to say -- Leroy Dennis  
4 again, Mr. Chairman, I would be glad to take that one on as  
5 part of our group. I do question whether or not that is a  
6 small business issue or just a general issue. I think it is  
7 broader than just the small business side of things.

8 MR. WANDER: Which particular issue, the  
9 materiality, the advice --

10 MR. DENNIS: No, the relationship and advice with  
11 the auditors.

12 MR. WANDER: Okay, that is a good idea. It should  
13 be under --

14 MR. DENNIS: Under item six.

15 MR. WANDER: Six.

16 MR. CONNOLLY: Mr. Chairman, one more time, I  
17 promise, James Connolly, a capital formation item. I think  
18 we need to take a very hard look at the real world  
19 implications of a number of U.S.-based companies, American  
20 companies being unable to attract capital in the United  
21 States and in point of fact turning to places like the  
22 alternative investment market in London. I was told  
23 yesterday that there is a junior exchange I am unfamiliar  
24 with attached to the Tokyo Stock Exchange where there are now  
25 some American listings. Certainly I am familiar with a

1 number of companies who have felt that they have needed to go  
2 up to Canada to access capital. And given the implications  
3 to the competitiveness and ingenuity and the impact on small  
4 business being able to attract that capital domestically, I  
5 would certainly like to look at what I am aware of being a  
6 prospective, essentially a merging markets exchange that is  
7 by no means universal but there is some movement on the  
8 American stock exchange to take a look at whether or not  
9 there is an interest level. The AMEX based in New York based  
10 in New York just this past week elected a board of governors.  
11 They are now an independent exchange again having brought  
12 themselves back from NASDAQ. And they are both looking for  
13 new business opportunities but also perhaps we can keep it  
14 home as opposed to having to shop it abroad. I would like to  
15 basically examine the needs to access international capital  
16 markets when in fact the smaller companies are often finding  
17 it difficult to do that here and whether or not we can  
18 perhaps recommend some solutions to that broader question.

19 MR. WANDER: I guess something like broader access  
20 to capital including foreign markets would be one way to  
21 describe that. Jim points out is there anything we should  
22 take off the agenda? Every one of these topics could, as I  
23 said, you could talk about materiality sort of forever and at  
24 the end of the day I guess it is really the courts who are  
25 going to be the final arbiter of what is material. But are

1 there any items again that we might want to think are low  
2 priority that we should delete or we can do this. When the  
3 subcommittees meeting informally, you can prioritize I think  
4 your items so that nothing falls off the list but you will  
5 attack the top 20 rather than the top 40 or whatever the list  
6 is.

7 MS. DOLAN: This is Janet Dolan. And I was just  
8 going to suggest the same because I think all of us that have  
9 served on commissions and advisory boards in the past know  
10 that well-intentioned scope creep is the nemesis of all good  
11 commissions. So I would just urge that each of the  
12 subcommittees have that opportunity to prioritize and then  
13 also that the whole advisory board be aligned on where we can  
14 best use our resources to be most effective.

15 MR. WANDER: I think you can't overemphasize that  
16 point because half a dozen really good recommendations that  
17 are adoptable and implementable are far better than 40  
18 recommendations that aren't well thought through.

19 MR. CLOUTIER: Mr. Chairman, Rusty Cloutier again.  
20 I want to go back to Scott's point again. I just received,  
21 and I would be glad to share it with the commission, a survey  
22 done by the North Carolina Banker's Association. And North  
23 Carolina I think we would all recognize has some of the  
24 larger banks in the country and some of the smaller banks.  
25 And it was a very interesting survey that the current cost of

1 being able to comply with accounting rules for the largest  
2 corporations, largest banks is about 1 percent of their  
3 earnings. But to smaller banks it has become 9 percent of  
4 their earnings. This has become a significant situation I  
5 think for smaller companies is that smaller companies having  
6 to meet these cost requirements are continuing to put a  
7 burden on them. So I think that is something we need to look  
8 at very carefully. And when you tell a smaller company,  
9 well, you can't go to your auditor to ask them questions, it  
10 costs a lot of money to go get another party to do the same  
11 thing when you are a very in my business non-complex filer.  
12 The business I am is making loans and taking deposits. I  
13 don't do options and arbitrages and all of this stuff. So I  
14 am much simpler to look at for an auditor than a larger  
15 company but yet the costs sometimes will be very strong. But  
16 if any of the committee chairmen would like, I would be glad  
17 to share those comments from that North Carolina Banking  
18 Survey, and I know they will be glad to send you a hard copy  
19 of what they have done.

20 MR. WANDER: In fact, if you could get it to Kevin,  
21 he will distribute it to everyone.

22 MR. BROUNSTEIN: Mr. Chairman, can I make a  
23 comment? This is Rick Brounstein. I was going to come back  
24 to 62 and say when we were talking about stock options is  
25 what we really need to do, you even referred to it, is the

1 concept that cash is king. And on so many of these things  
2 that I am hearing right now seem that they are very  
3 interrelated with these issues. If we simplified the  
4 accounting and we looked at what was important for little  
5 companies, how are they evaluated. Everyone wants to know my  
6 burn rate, they don't really care how I account for warrants  
7 or stock options. And when I raise capital, they don't care  
8 whether it goes in debt or equity, they want to know I got  
9 another \$5 or \$10 or \$15 million. And so many of those  
10 things, if we solve those, I think we are going to find that  
11 there are going to be a few larger pieces. And I would  
12 suggest within the accounting rules, it is sort of the cash  
13 is king concept that will simplify a lot of the issues. A  
14 lot of the reasons why I have to go now and talk to another  
15 accountant because I can't talk to my auditors, it is not on  
16 the basic accounting that produces my cash statements, it is  
17 on the accounting for warrants or stock or some of the new  
18 FAS-150 or some of these new EITF's that seem to keep rolling  
19 out.

20 MR. WANDER: We will add something to that effect  
21 to accounting principles. Yes, Mark?

22 MR. JENSEN: Mark Jensen again. One thought that I  
23 would like to add, I don't want to add something more to the  
24 agenda because I think it is getting full. It is past full.  
25 But I think it is implicit in a lot of this but I would like

1 it to be explicit within each one of the subcommittees that  
2 when we are talking about public companies, I would also like  
3 there to be a discussion around companies about to go public  
4 or thinking about going public and whether there should be  
5 specific relief under certain rules for those companies and  
6 how we might be able to make it easier for companies going  
7 public to access public capital markets without making a huge  
8 investment in infrastructure prior to actually taking the  
9 company public.

10 MR. WANDER: In fact, someone commented to me that  
11 Sarbanes-Oxley, once you file a registration statement to go  
12 public, you are public. And not everybody makes the journey  
13 to a closing and so they are in the box at least at that  
14 point. So that is an area.

15 MR. JENSEN: I would like us as we go through this  
16 think about the impact that maybe this is having on the  
17 private capital markets as well in terms of the exits for  
18 venture capital firms, in terms of a lot of business  
19 strategies include accessing the public capital markets and  
20 whether or not these rules are forcing a change in business  
21 strategy I think would be a good topic.

22 MR. WANDER: Well, the whole phenomenon of going  
23 dark versus going private versus essentially merging instead  
24 of going public and the implications of all of those on  
25 frankly the economy.

1           MR. JENSEN: And I think the availability of  
2 opportunities for individual investors to invest in those  
3 companies that choose not to go public but rather get  
4 acquired.

5           MR. WANDER: Any other comments? Alan, would you  
6 mind, do you have sort of an overview of what we have just  
7 been through to sort of see what we are missing or what we  
8 should add?

9           MR. BELLER: No, I don't really have any comment.  
10 I agree with you that every one of these issues is an  
11 important one and in a world with infinite time and  
12 resources, this committee would deal with them. My reaction  
13 to the agenda, even as originally presented this morning, was  
14 the same as yours and other members of the committee, which  
15 is that it was already certainly an ambitious and perhaps an  
16 overly ambitious list. I think these changes, none of which  
17 I would have any quarrel with as interesting topics, merely  
18 make it more overly ambitious. And I think what that does is  
19 make it incumbent on the committee and in the first instance  
20 on the subcommittees and then in the committee to make a  
21 serious attempt to prioritize things and work on the ones  
22 where you think the impact for "smaller public companies" is  
23 greatest.

24           I would also echo the point, I think a lot of what  
25 has been mentioned or some of what has been mentioned, the

1 issue of materiality under 404, for example really is an  
2 issue that is across the board and not limited to smaller  
3 public companies. I think the impact of the definition may  
4 be greater on smaller companies because the impact of the 404  
5 exercise itself is greater on smaller public companies. And  
6 I think in prioritizing what you want to focus on, I think  
7 maybe one of the things to look at is where is the committee  
8 really going to be focusing on its energies on things that  
9 are special to smaller public companies that might not  
10 otherwise get the attention as opposed to things that in fact  
11 impact smaller companies but impact them as part of the  
12 overall universe. But I have no quarrel with adding any of  
13 these things. I just think you ought to look at your  
14 calendars when you are thinking about how many of them you  
15 can do. And, as I said before, I don't think it is our place  
16 to give you a whole lot of direction on what to focus on so  
17 long as they are plausible and reasonable subjects because  
18 with the talent around this table on the committee, the  
19 reason we have you and have asked you to do this is so that  
20 you can give us your advice and we don't really want to get  
21 in the way of that.

22 MR. WANDER: Are there any other comments,  
23 suggestions?

24 MR. CONNOLLY: Mr. Chairman, if I could just speak  
25 to Mr. Beller for a moment on that subject.

1 MR. WANDER: It is Drew Connolly speaking.

2 MR. CONNOLLY: I am sorry, Drew Connolly. We are  
3 all very pleased and honored to be volunteers to move our  
4 agenda items, to contribute to the common wheel in the public  
5 discourse and hopefully provide some solutions. I am aware  
6 that there is an authorized budget in support of this  
7 committee. I suspect largely that would be for the human  
8 resources that Mr. Laporte would have available to him. I am  
9 wondering however whether or not the four subcommittees in  
10 fact would have the latitude or the leeway to engage subject  
11 matter experts to assist us in doing our role or whether that  
12 is not in our purview?

13 MR. WANDER: I actually don't think it is in our  
14 purview at this point. But if someone wants to raise that  
15 issue, we obviously could address it. Is that correct, Alan?

16 MR. BELLER: I think that is right. Both parts of  
17 that answer I think are correct.

18 MR. WANDER: Before we close this discussion, Jim  
19 and I set out some over-arching principles. And let me  
20 repeat those and add one to that. Those are first to further  
21 the commission's investor protection mandate. Second, is to  
22 seek cost choice benefit inputs. Third, is to keep it  
23 simple. Fourth, is to maintain a culture of  
24 entrepreneurship. And, fifth, is capital formation should be  
25 encouraged. I am going to add another one and that is we

1 must prioritize our recommendations because having been  
2 through exercises like this in the past, I know that  
3 everybody has an agenda item that they think is absolutely  
4 crucial and it is important. But the fact is we only have a  
5 certain amount of time and resources, and we will have to not  
6 deal with every issue. And, as I said, that doesn't mean at  
7 the end of the day we can't put a list of open items that we  
8 suggest another commission or another committee or the SEC  
9 itself take on. So they don't drop off the face of the  
10 earth. They just don't get done by us.

11 MR. BELLER: I will give you an example of that,  
12 Herb, if I can break in for a second. I think the question  
13 of materiality is something certainly at least in connection  
14 with 404 I would not dare to pre-judge what the commission or  
15 staff or the PCAOB board or its staff would come out, but I  
16 think that is an issue that in the broader sense not limited  
17 to smaller public companies is something that we certainly  
18 will be considering in the coming weeks and months.

19 MR. WANDER: Yes, Janet?

20 MS. DOLAN: Mr. Chairman, my question as the chair  
21 of the 404 is that is a, yes, we are interested in it, we  
22 could use your help or there will be other forums in which it  
23 will get a much better airing and leave it to them?

24 MR. BELLER: No, I think it is the former rather  
25 than the latter but I think in terms of thinking of where you

1 want to put your resources, one of the things that the  
2 subcommittees and the committee probably ought to want to  
3 consider is sort of what other energies of what other people  
4 are going to be devoted to it. I think that is the point  
5 that Herb was making.

6 MR. WANDER: And I guess Jim reminded me, and I do  
7 now think we ought to mention part of our charge and our  
8 over-arching principles to see where if possible there is a  
9 break point to have a differential regulation for smaller  
10 businesses. And I use smaller rather than small because we  
11 really have to address the question of what that means. We  
12 have set out, there are some break points that exist in the  
13 law today and a proposed one with companies of over \$700  
14 million in non-affiliated market cap. So there are  
15 breakpoints. The real question is, and we have it on the  
16 agenda, but I am just emphasizing it, are those the right  
17 ones? Is market cap the right metric or should there be some  
18 other metric? Should it be risk-based not size-based? And  
19 what kind of meaningful regulation can you have? I know for  
20 example people have not used the small business sort of  
21 regimen which has under \$2,500,000,000 because there are not  
22 that many companies and while the regulations are I guess  
23 less onerous, they still are formidable. And I think many at  
24 least securities lawyers would just as soon follow the  
25 regular procedures, it is just as easy as the less onerous SB

1 regulations. So part of our charge is also to really address  
2 what are smaller businesses and how can we make a meaningful  
3 difference in their regulation.

4 With that we are actually very early but I think we  
5 can take a break now. Our subcommittees are going to meet  
6 informally and discuss now based on this full discussion of  
7 what their agendas are, how to organize themselves and they  
8 will report back to us after the break at 1:30. And we will  
9 call on each of the subcommittee chairs to give us a brief  
10 report on what they decided and how they are going to  
11 operate. And then we will discuss factual input needed and  
12 then turn to our timetable. So unless there is anything else  
13 anyone would like to raise? Yes, Alan?

14 MR. BELLER: I just would raise a procedural point.  
15 Given that we are a little ahead of schedule on the agenda  
16 and the afternoon looks fairly full, would you like to have  
17 people come back at 1:00 instead of 1:30 and start again half  
18 an hour earlier?

19 MR. WANDER: That is probably a good idea, yes.

20 MR. LEISNER: If I might interrupt, we had lunches  
21 scheduled to be delivered at 11:30 and it doesn't look like  
22 they are here yet, so I think what we are going to need to do  
23 is people go off to the meetings and then maybe take a break  
24 in their meetings and come back here at 11:30 to pick up  
25 their lunch and then go back up to the meetings rooms, if

1 people don't mind doing that.

2 MR. WANDER: That is fine. Why don't we begin at  
3 11:00 with the informal meetings, come down for lunch around  
4 11:30, bring your lunches back up to the room and then we  
5 will reconvene at 1:00. Thank you.

6 (Lunch break.)

7 MR. WANDER: I hope everyone had a pleasant lunch  
8 break and that all of the informal meetings of the  
9 subcommittees proceeded very well. I did sit in on two of  
10 them and I know Jim sat in on a couple and Alan Beller and  
11 the chairman came around to visit us. So I hope they were  
12 productive. And we would like to hear the feedback so that  
13 we can move ahead with our overall goals. And I will first  
14 call on Steve first on the disclosure and governance  
15 subcommittee.

16 MR. BOCHNER: Thanks, Herb. Well, we had a very  
17 good full discussion I think of the topics that were in our  
18 agenda summary, and I have to say I was impressed with the  
19 input from our subcommittee, I think some great ideas. The  
20 first thing we talked about was this concept I brought up  
21 this morning about whether we should look at the problem of  
22 late filings and filing deficiencies and the CEO/CFO  
23 certifications and whether there is something that can be  
24 done there to allow companies to follow. Is that a good  
25 idea? Should companies be allowed to put the information out

1 there? And to what extent do the certifications need  
2 modification if that in fact happened? So we talked about  
3 getting more data on this to look at both from the SEC and  
4 perhaps get information from the SROs about how big of a  
5 problem is this, what do the late filings, the deficient  
6 filings look like. And so we are going to have more  
7 discussion on that topic after that fact finding.

8           We then spent a considerable amount of time  
9 discussing the definition of smaller public company. And we  
10 looked at the BSB definition and that was, I think everybody  
11 thought that in today's world very low for our purposes. We  
12 looked at the accelerated filer, \$25 million market cap, and  
13 I think the sense of the subcommittee was that also is a  
14 fairly low number and that companies with market caps in  
15 excess of that still were smaller public companies in the  
16 view of many of us and so we wanted to do more work there.  
17 We think we had an upper range of \$700 million clearly was  
18 the well known seasoned issuers and the 33 Act Proposal  
19 probably provides an upper range on what a smaller public  
20 company can be. And so something within that ban kind of  
21 framed it, and we want to do more work there.

22           One of the subcommittee members recommended that we  
23 look at other types of indices like the Russell 3000. So we  
24 are going to look at other ways at getting at the definition  
25 of smaller public companies. We talked a little bit about

1 risk-based proposals but we went back to Herb and Jim's  
2 thinking about trying to keep it simple and keep it  
3 objective, and we are hoping that we can have a more elegant  
4 and simple, more objective criteria for smaller public  
5 companies. So we are going to do some more work there, and I  
6 think we are going to need to collaborate with some of the  
7 other subcommittees on some of the information they are  
8 gathering about the cost of compliance and so on and figuring  
9 out where that threshold should be. As a percentage of  
10 revenue, where is 404 and where is really the right place to  
11 draw those lines. So I suspect we are going to do a lot of  
12 work there and more to come.

13           We then transitioned to once we got the definition  
14 of smaller public companies and working with the other  
15 committees, then to our core subject matter of the governance  
16 and disclosure subcommittee. What should be the relief that  
17 we want to look at that we should recommend. And so we first  
18 talked about the core governance requirements, the audit  
19 committee requirements found in Sarbanes-Oxley, the SRO  
20 requirements from NASDAQ and the New York Stock Exchange  
21 regarding the levels of independence. And we want to do more  
22 work there and more fact finding about the costs and the  
23 burdens associated with that. But I think the sentiment was  
24 that that does not appear to be where a lot of the concern is  
25 among the companies that we all on the subcommittee have

1 exposure to. So I think we need to reach out and find out if  
2 in fact the independence criteria, the audit committee  
3 requirements, the audit committee financial expert and code  
4 of ethics disclosure, those what I call the core governance  
5 requirements really are causing an issue out there or not  
6 and, if not, we want to move on and spend our time on things  
7 that are higher priority. But we do want to take a look at  
8 those items.

9           We then moved into the disclosure area, and again  
10 noted that the SB form was probably -- to the extent that  
11 there needed to be some relief in the area of 33 Act  
12 disclosure and 34 Act disclosure that the SB thresholds  
13 probably were too low. And so we asked ourselves should we  
14 spend time thinking through what kind of relief should be  
15 granted, should we have a SB form that dove-tails with this  
16 definition of smaller public company that we have been  
17 talking about, and exactly what kind of relief, if any, is  
18 appropriate.

19           And then we covered a couple of final topics. We  
20 looked at the loan prohibition in the legislation and noted  
21 that in some cases there seemed to be legitimate business  
22 reasons to make loans, such as relocation loans, and some of  
23 the other topics that have gotten a lot of air time such as  
24 "cashless" exercise programs and perhaps insurance and other  
25 areas. And so we are going to take a look, if you all agree,

1 at whether there is -- and we are going to do this cautiously  
2 because I think there was concern about making too many  
3 exceptions here -- but whether there should be an effort to  
4 carve out some exemptions from the loan prohibition for  
5 legitimate business purposes and appropriate situations. So  
6 I think that summarizes our discussion.

7 MR. WANDER: Fine. Are there any questions of  
8 Steve? Anybody on that subcommittee like to add anything?

9 MR. JAFFEE: I would just like to make a quick  
10 comment on this size deal. We discussed that it would be  
11 good to come up with something that would be expandable over  
12 the years, not a finite number necessarily which could become  
13 obsolete and that is why we were interested in an index like  
14 the Russell 3000 as a benchmark.

15 MR. WANDER: Why don't we go next to the internal  
16 controls over financial reporting. Janet?

17 MS. DOLAN: Thank you very much. First of all, I  
18 would like to thank all of our team members, Rich and Alex  
19 and Deborah and Kurt, and Mark Jensen has also joined our  
20 subcommittee. And then Daniel is our official observer. So  
21 we worked very hard so I want to acknowledge the  
22 contributions of all of them.

23 We started out I think rightfully sort of  
24 acknowledging the environment we are in, which is we are  
25 cognizant that the SEC and the PCA will be taking written

1 comments and they are holding their roundtable tomorrow. So  
2 we are going to work obviously in parallel but we are going  
3 to be very cognizant of what is coming out of that. There is  
4 no use duplicating efforts or having wasted efforts. So if  
5 we start to get the impression or start to fill that some  
6 significant changes are coming as a result of that that may  
7 affect all companies, it reduces the efforts we have to do on  
8 behalf of small companies. So we just acknowledge that that  
9 is an important process to keep our eye on and to work with  
10 in parallel.

11 We also acknowledged that it is an important  
12 process that we don't want to ignore either in terms of  
13 timing. So we talked about the opportunity to make some  
14 initial recommendations, if we would have a fair amount of  
15 alignment early on in the process so that we could get them  
16 in to help influence that process if it were appropriate,  
17 recognizing that we don't want to trade off quality for  
18 haste. So there is no expectation that we will do anything  
19 hastily but if we have alignment around anything early on, we  
20 will certainly take the pace of that other process in mind as  
21 we do our work.

22 We divided our work just as the previous committee  
23 focused on the areas they think are most important. I think  
24 particularly in the area of 404, everyone has an opinion. I  
25 think everybody has an idea of where they would like it to

1 end up, they just aren't sure how we are going to get there  
2 from here. So we had to spend a fair amount of time just  
3 getting through expectations and hopes and aspirations and  
4 then try to get convergence around what would be a process  
5 that might actually bring all of this together in some  
6 meaningful recommendations. And so we are going to focus on  
7 five areas, it is early. We only obviously had one meeting  
8 but we are trying to segregate our work into five main areas,  
9 and the over-arching premise or goal of our work is to say if  
10 we believe that we could make recommendations that would  
11 certainly maintain investor protection, but yet eliminate  
12 some of the activities currently required that don't provide  
13 enough value in light of the tremendous cost in either money  
14 or time for small companies, how might we approach that, how  
15 might we start to identify different ways of looking at the  
16 current structure and reshape that structure so it better  
17 fits small companies. So that is what we tried to do, what  
18 would be different cuts that we could take of this and try to  
19 get to some recommendations that really are tailor-made for  
20 supporting the recognized differences between small companies  
21 and large companies and still protect the investor.

22           And we acknowledge that it will be the work of this  
23 entire advisory committee to deal with the issue of size, but  
24 I think as we just heard in our previous brethren  
25 subcommittee, I think all of us are kind of coming at size

1 from a different need but we are all going to have to  
2 reconcile it. But we are looking at at least five different  
3 ways that we might approach the question of how do you peel  
4 this onion and get to what is really necessary for small  
5 companies and what might be eliminated for small companies.

6           The first approach would be to try to take a risk  
7 approach. That is, can we try to identify those controls  
8 that are most critical for all companies, small or large, but  
9 can we also identify some controls that are currently  
10 required but probably aren't as critical for small companies.  
11 So can we do some kind of risk assessment and prioritize and  
12 draw the line somewhere along the continuum of where it is  
13 today based on a risk assessment. And a subset of that will  
14 be particularly in the area of the IT controls as a special  
15 example of that.

16           A second cut we will try to make is on size, just  
17 as I said. Is there some way that we could look at drawing  
18 the line on size based on revenue, on market cap, or on some  
19 other clearly defined metric that everyone would know whether  
20 they were on one side or the other of the line.

21           The third is could we make some recommendations  
22 around the timing of the certifications. That is could we  
23 make recommendations that some of the testing could be done  
24 throughout the year and take some of the burden off those  
25 scarce resources at the end of the year, could we make a

1 rotation schedule that might say that everything has to be  
2 tested at least every three years but one third of them every  
3 year, anything around rotation or timing that could reduce  
4 some of the expense and pressure on small companies.

5           The fourth is we look at what we call autonomy but  
6 are there certain testing of controls that could be done by  
7 the company and that the auditor could rely on as opposed to  
8 duplication of effort where first of all the company has to  
9 test everything and then the auditor has to go through and  
10 test everything as well. Is there any way that we could  
11 segregate some of those and allow a reliance on the company  
12 testing.

13           And then the fifth one is we called it sort of  
14 special needs, and those might be IPO companies or other  
15 companies. It might be one year grace period when you put in  
16 a new IT system. Just are there some unique or special needs  
17 of small companies that we should be making specific  
18 recommendations on, even though it may not result in drawing  
19 the line for a particular category or not.

20           So we have assigned our work. Everybody has  
21 stepped up to the plate and volunteered to head one of the  
22 five and then we are each all working on as sub-group  
23 members, and we are setting fairly aggressive timelines for  
24 ourselves. So we are looking in the next few weeks to take  
25 our first cut at recommendations and see if we can get, what

1 our first look at recommendations and alignment around them  
2 might look like.

3           We concluded then with the very last question, and  
4 perhaps everyone of the subcommittees has this question, but  
5 when we make recommendations, if some of them are not  
6 completely within the purview of the SEC but might be in the  
7 PCAOB or some other entity, how do we ultimately deliver a  
8 work product here in which we give the best recommendations  
9 we can and then ensure that they get to the appropriate  
10 bodies and what the role of the SEC might be in supporting us  
11 in that.

12           MR. WANDER: Are there any additions by any of the  
13 subcommittee members or any questions by any of the other  
14 committee members? Okay, if not, why don't we go to  
15 accounting standards. Leroy?

16           MR. DENNIS: Thank you. We had a very similar  
17 discussion around size and actually I think would recommend  
18 that the committee come together as a group and determine  
19 what kind of size parameter we are going to be looking at  
20 because we didn't think it was appropriate for our committee  
21 to have a size of small being \$30 million and somebody else  
22 have \$75 or \$100 or something like that.

23           As far as our priorities, our first priority we  
24 looked at was really the whole over-arching question of big  
25 GAAP versus little GAAP and we thought everything else kind

1 of drove down underneath that. And really breaking that down  
2 into measurement recognition and disclosure as the three  
3 basic areas that need consideration of cost versus benefit.  
4 And I would also throw in simplicity with that.

5 I think the initial thoughts of our groups is that  
6 recognition areas of GAAP would be difficult to apply  
7 different standards of recognition for different size  
8 companies but clearly that there was some flexibility in the  
9 measurement and disclosure areas that we ought to consider.  
10 We are in the process, and we have signed out a list of users  
11 and are going to develop some questions for those users. One  
12 of our big concerns is that if we were to come up with  
13 different recommendations for small companies that say the  
14 investors or the users of the financial statements would  
15 ignore those and require their companies to file under big  
16 company standards and defeat the process. So we are  
17 cognizant of what the concerns of the users of the financial  
18 statements are and somewhat similar along the lines of the SB  
19 discussion that was held earlier today about whether people  
20 would be required to go to a bigger standard if that existed.

21 We would like to develop a list of questions and  
22 then use the website, and I think we are going to talk about  
23 that later on as to using that as a tool to solicit input.  
24 And we have scheduled kind of a gut check call in a couple of  
25 weeks to see where people are at on developing those

1 questions and talking and so we can bring those out to the  
2 investors or to the other users of the financial statements.

3           We then went on to talk about the other areas of  
4 our committee. When we talk about specific accounting  
5 standards, and again should we make any recommendations in  
6 that area around measurement or disclosure. Ultimately,  
7 those recommendations we felt had to go to FASB staff since  
8 they are the ones that set accounting standards and so we  
9 think it is important to get their buy in into this process  
10 sooner rather than later. And again looking at areas for  
11 small business that we can make it maybe not different but  
12 easier to measure. And then maybe some relief from  
13 disclosure for the smaller business and maybe not so much  
14 different in the recognition area itself.

15           On item 6.3 of our agenda, we didn't put a lot of  
16 priority to that. In fact, would recommend we remove it from  
17 our consideration because again setting accounting standards  
18 is going to be the FASB's staff job. We see our job to  
19 recommend suggestions to the FASB staff with hopefully the  
20 SEC's support behind that. So we would recommend taking that  
21 off. We would add to our agenda though that we deal with  
22 effective dates and transition rules for small business and  
23 can we come up with some over-arching principles in total  
24 that the FASB staff and the SEC can use as guidance when we  
25 adopt not only our current accounting standards that are out

1 there but the next five years of accounting standards that  
2 will be looked at.

3 We didn't spend a lot of time dealing with the role  
4 of auditors, although we talked a little bit about it. And  
5 so that is something we are going to have to deal with down  
6 the road. Again, our first priority being the over-arching  
7 principle of big GAAP versus little GAAP. So right now we  
8 have got a list of assignments out to the people as far as  
9 developing questionnaires. We are then going to get back  
10 together in a couple of weeks, finalize those, and hopefully  
11 gather some input then and use that to come back together in  
12 a formal meeting and give our first recommendations.

13 MR. WANDER: Thank you, Leroy. Any additional  
14 comments or questions? If not, we will go to our final  
15 subcommittee dealing with capital formation. Dave?

16 MR. COOLIDGE: Everything we talked about has been  
17 covered. Our committee had a lively discussion about a  
18 number of topics, one of which everybody else did cover which  
19 is the size definition question. I think our desire is like  
20 everyone else's, to try and get some common ground there.  
21 The idea being that once we define what is a smaller business  
22 or a small business, that we can talk about various potential  
23 forms of regulatory relief for that category of company.  
24 Many of the things we talked about were similar to what other  
25 committees talked about with respect to 404 compliance,

1 filing deadlines, attestation, by whom and the scope, the  
2 materiality test, and the 404 requirements. Talked about  
3 governance relief in the sense that perhaps the number of  
4 independent outside directors, the definition of an  
5 independent director, et cetera, would be helpful to smaller  
6 companies if they had a little more leeway, audit committee  
7 makeup, perhaps not 100 percent independent directors as  
8 defined, and the time to transition both from a reporting  
9 standpoint but also from a governance standpoint would be  
10 helpful for smaller companies if they had more time to do  
11 these things. And the idea of rotation, not having to do  
12 everything all at once, instantaneously.

13           Then the other issues that we talked about really  
14 relate a lot more to the capital formation process and what  
15 has happened over the past few years and really over the last  
16 many, many years as increased rules and regulations and  
17 standards have been put forward by regulatory agencies and  
18 SROs, the access to the public markets is more difficult.  
19 Companies have to be larger, they have to be more  
20 sophisticated. They have to have different governance in  
21 place today that they may not have been required to have 10  
22 or 15 years ago. And so the hurdle is just going up and up  
23 and up for companies that want access to the public markets.  
24 Now that be fine and we did talk about the role of private  
25 capital. There has been a significant increase in the

1 availability of private capital and as a result the capital  
2 needs of these smaller companies may be getting met but the  
3 smaller ones probably aren't having it met in the public  
4 markets. So that is just an environmental issue. It also  
5 relates to the access to accounting resources, the  
6 requirements that so many investors have for Big Four  
7 accounting, underwriters demanding the same thing, not  
8 wanting to take the company public unless it has got a Big  
9 Four accounting opinion and the difficulty for small  
10 companies to pay those fees and to get the time and attention  
11 of a large accounting firm.

12           Role of investment bankers, same issues, wanting  
13 bigger companies, bigger deals in order to justify the time  
14 and expense, the ongoing investment that they have to make in  
15 a company, especially if they are going to pick it up in  
16 research. These are all issues that relate to how a company  
17 gets public and whether there is a bias now against companies  
18 going public, whether they would prefer to just sell the  
19 business for a liquidity event as opposed to going public  
20 because of all of the regulatory hurdles.

21           Many of these things we can't do much about, it is  
22 just a fact of life. But I think as a general matter, the  
23 increased hurdles that companies have to get over in order to  
24 get public are probably causing bigger, more mature companies  
25 to go public than might have been the case 10 or 15 years

1 ago.

2           Increased liability exposure for officers and  
3 directors, another obstacle in the way of capital formation  
4 in the public markets. Again, we weren't saying this is  
5 necessarily bad. Public markets have a role to play.  
6 Private markets have a role to play as well and perhaps  
7 between the two the job is getting done. There is a fair  
8 amount of capital out there that can be accessed, it is just  
9 that you have to go about it in different ways for different  
10 companies.

11           So our focus going forward I would say is to look  
12 to see if there are any things that we can do for the smaller  
13 companies to make it a little bit easier to go public and to  
14 stay public. There are a lot of existing public companies  
15 out there that are really struggling with complying with a  
16 lot of these regulations and may be forced to sell the  
17 business or something else, go private in order to avoid the  
18 cost and the expense. But we will be looking at the  
19 accounting resource issue, the investment banker resource  
20 issue, private capital resource issue, and then coming back  
21 perhaps with some certain regulatory relief recommendations  
22 that may overlap with other committees but we will just have  
23 to coordinate that at the end of the day.

24           MR. WANDER: Thank you, Dave. Any questions,  
25 comments, additions? I think it is obvious that everyone

1 grappled with the size problem and that we probably will have  
2 to attack that issue on a committee-wide basis. And I wrote  
3 that down, Jim, and that will be one of the things we will  
4 try and exert leadership on so that everybody can be dealing  
5 with the same issue. And then of course once we do that, and  
6 I would say we probably ought to establish it in sort of a  
7 tentative fashion and then see what it is that you can then  
8 do for companies falling under that criteria, to see whether  
9 it is helpful to them and whether it continues to provide  
10 investors with the information they need to make investment  
11 decisions because if they fall off the cliff and don't  
12 provide information, we probably will be counterproductive in  
13 that scope.

14           So I think, at least the way I listened to what all  
15 of the subcommittees did, that we have an excellent start on  
16 our project. I know all of you have scheduled meetings,  
17 which you can do, I am going to repeat this, obviously if you  
18 all want to get together in person you can but knowing that  
19 terribly time-consuming is hard and expensive, conference  
20 phones. And if you really want to see each other, I think  
21 the SEC has some telephone conferencing systems that you may  
22 use if they are available from their regional offices. So  
23 that could be another method of communicating before our next  
24 full committee meeting.

25           The next item on the agenda is discussion of

1 factual input needed. All of you talked about getting more  
2 information and there are a number of ways that we can do  
3 this. The first is we will be publishing our agenda in the  
4 next few days, as soon as it gets brought up to date with the  
5 items we added this morning. And then that will be published  
6 in the Federal Register and put on our web page. People will  
7 be asked for comments to be supplied in the next 30 days, so  
8 we may get some additional input from that.

9           A second method is I am going to talk about  
10 questionnaires. Again, if any subcommittee or the whole  
11 committee decides that there are discrete areas or even large  
12 areas in which you would like to put out requests for public  
13 comment, the subcommittee chairs should get those to us. We  
14 will obviously consider them very seriously and again by the  
15 use of our web page ask for comments to various  
16 questionnaires. It might be a little early to be doing that  
17 but it might be useful to decide what are high priority items  
18 from low priority items.

19           The next area is either hearings or roundtables.  
20 The SEC is holding a roundtable tomorrow. I personally view  
21 those as being very important because I think they validate  
22 the process in that we have gone out to the community of  
23 people involved and asked for their opinions. And I think it  
24 adds credibility to the final product. And there are  
25 inexpensive and fairly informal methods of doing that. We

1 could do it around the country. The whole committee doesn't  
2 have to come. It could be a subcommittee project. It could  
3 be two subcommittees or it could be a committee project. But  
4 we should consider and talk about during the time between now  
5 and our next full committee meeting the subject of whether we  
6 should have roundtables and/or hearings and that could be at  
7 two or three places in the country. I would strongly urge  
8 that if we did that, we obviously have to set ground rules so  
9 that we are not there from 6:00 in the morning until 6:00 at  
10 night. But in my experience they are really -- you wind up  
11 not having as many people as you think you might have to  
12 present and that anybody who does present should be required  
13 to produce a written statement. I think that makes the  
14 record very clear, and I think it provides more sound  
15 thinking on the part of anybody who wants to come and present  
16 their views.

17           The other two sources are the SEC's Office of  
18 Economic Analysis. And we do have someone from there who  
19 could give us a little bit of background on the SEC's office  
20 and the services that are available to everyone.

21           MR. BELLER: Okay, just for the members of the  
22 committee, joining us at the table is Chester Spatt, who is  
23 the chief economist of the SEC and runs our Office of the  
24 Chief Economist. There are a couple of representatives of  
25 his office who have been with us today also listening in.

1 But I am going to give the floor to Chester to talk about  
2 resources and the work of the office and so forth.

3 MR. SPATT: Thank you, Alan. The Office of  
4 Economic Analysis at the Commission very much appreciates  
5 that the attention that the panel will draw to the important  
6 questions of how regulation affects the ability of operating  
7 companies to access the public markets, focusing on small  
8 business, we understand that some of the Sarbanes-Oxley  
9 reforms have raised questions about how the reforms are  
10 specifically affecting small business and what might be done  
11 to help mitigate any undue burden. We also recognize that  
12 the evidence on some of these effects is not always clear,  
13 which clearly calls for careful examination of research  
14 reports and academic studies as they continue to emerge.

15 It is important I think that we try to accommodate  
16 the special circumstances of small business, even absent  
17 issues of past burden. One context where our office has been  
18 directly involved in that sort of issue has actually been in  
19 the context of options expensing. We have worked very  
20 closely with the Office of the Chief Accountant at the  
21 Commission on the implementation of FAS-123R, which requires,  
22 as you know, the valuation and expensing of employee stock  
23 options. I understand that there are concerns about some of  
24 the special issues, concerns were expressed this morning in  
25 fact by you about some of the special issues involving

1 employee stock option expensing. One of the things that we  
2 did as part of our work in option expensing in fact was to  
3 try to identify some of the key issues as they relate to  
4 small business, and specifically in many cases the absence of  
5 traded options obviously in the case of small business and  
6 what the import of that would be for the valuation process.  
7 And we made recommendations as to how to attempt to port the  
8 options approach given that expensing is now required to the  
9 context of small business.

10 I think the panel obviously represents  
11 opportunities that extend well beyond Sarbanes-Oxley and well  
12 beyond the options expensing issue. Obviously, the public  
13 markets are evolving and it is important that small business  
14 have potential access to that. And I think there is a  
15 broader, there has been a broad research agenda on some of  
16 these issues that I think our office can potentially help you  
17 tap into it.

18 Now I see that the role of our office and the  
19 expertise of our office is quite varied. I think one of the  
20 things that we are very good is at evaluating the economic  
21 consequences of different policies. We are involved actively  
22 in the Commission in helping to try to formulate efficient  
23 rules and certainly our work I think in the options expensing  
24 area today has been an attempt to try to do that. At the  
25 same time, we are also good at analyzing data and

1 understanding the market processes in which data arises and  
2 understanding the import of that. On our staff we have  
3 almost 20 Ph.D.'s who are trained in economics and who help  
4 support the various parts of the Commission, including of  
5 course as I referred to the Division of Corporate Finance and  
6 the Office of the Chief Accountant.

7           Among the types of issues where I see our expertise  
8 as being particularly germane would include the following.  
9 In the case of 404, clearly there are various concerns about  
10 the ability to comply with 404 and the complications  
11 associated with the compliance. I think subject to the  
12 availability of data, we are certainly prepared and I think  
13 interested in trying to help you assess those issues. They  
14 are starting to be data available now with the first filings.  
15 I think that is potentially, it is clear from the broader  
16 feedback that we have observed at the Commission that the 404  
17 issue is clearly a very important issue, and there may be  
18 obviously particularly important concerns in the small  
19 business area with respect to 404.

20           The issue of capital formation is clearly a very  
21 important issue. We have some ongoing projects in that area  
22 and we have a lot of internal expertise in this area. One of  
23 our staff members, who is in fact going to be our lead person  
24 on this project, Kathleen Hanley-Weiss, who is seated toward  
25 the back, is in fact in her prior work previously as a

1 professor at the University of Maryland was one of the  
2 leading experts in fact on the IPO process. So we have a lot  
3 of expertise and understanding of various aspects. We also  
4 have a lot of expertise on other aspects of the capital  
5 formation process. And we recognize that the issues and  
6 needs of small business maybe somewhat different.

7 I think our office is also in general very  
8 knowledgeable about academic studies done on various aspects  
9 of the issues of interest to you. And I think we are in a  
10 good position, our staff is well read, and I think in a good  
11 position to evaluate the academic research that is out there.  
12 I think we certainly want to work closely with you, and I  
13 think we have a lot of skills and expertise both with respect  
14 to our knowledge and ability to evaluate the existing  
15 academic literature with our ability I think to help  
16 conceptualize issues and understand the competitive market  
17 processes and our skills in understanding and working with  
18 data.

19 So a few moments ago I introduced Kathleen, I also  
20 want to just take a moment my other colleague who is here,  
21 Cindy Alexander. Cindy is the assistant chief economist for  
22 Corporate Finance and Disclosure. And Kathleen and Cindy  
23 will be taking leading roles in working with your committee.

24 MR. WANDER: Thank you very much. We will have to  
25 develop the process for working through you and your entire

1 staff but primarily through Kathleen and Cindy, which we will  
2 have to -- so you are not bombarded by all sorts of different  
3 phone calls, sort of coordinate all of that, which I think we  
4 will do. But are there any questions of Chester while he is  
5 here.

6 MR. DENNIS: Mr. Chairman, Leroy Dennis, I have one  
7 question. Chester, given that we don't know what you know  
8 right now, and we are certainly not inclined to reinvent the  
9 wheel with surveys and other information, I was wondering if  
10 you had resources available that would summarize maybe the  
11 last three to five years worth of studies that might be  
12 applicable to the different subcommittees to this group?

13 MR. SPATT: We will certainly review that, and I am  
14 sure we will be in a position -- I don't know whether we will  
15 be in a position to do that across the board but I do  
16 anticipate certainly we will be able to do that with respect  
17 to many of the domains you will be working and we will  
18 certainly try to do that.

19 MR. DENNIS: Thank you.

20 MR. WANDER: Any other questions?

21 MR. CONNOLLY: Mr. Chairman, Chester, I would be  
22 particularly interested, I came to find today in our  
23 subcommittee meeting that there are probably a couple of  
24 thousand SB2 filers within the universe of public company  
25 reporting companies. Have there been any quantitative

1 extraction of data from those filers such as average  
2 revenues, such as average market cap, high/low, numbers of  
3 stockholders, or any of those kinds of things in terms of the  
4 impacts broadly and widely to the capital markets of the SB2  
5 filers?

6 MR. SPATT: I am not specifically aware of such  
7 extractions or studies but we will certainly check on that.

8 MR. CONNOLLY: Appreciate it.

9 MR. DAVERN: Alex Davern. I had a similar question  
10 as to the results of the early reports on 404 and  
11 particularly those who have filed proxies already, has the  
12 Commission had a chance to take a look at any cost data  
13 related to that based on size, either those who have failed  
14 the test or those who have passed. It is an area where our  
15 subcommittee has been tasked to take a direct look at, and I  
16 am not sure if any work has already been done on that that we  
17 can leverage as a starting point to consider the topic or if  
18 that is just something that we just need to engage you on to  
19 look at directly?

20 MR. BELLER: Alex, there has been work done in that  
21 area. It is ongoing. It is really being done more in the  
22 Office of the Chief Accountant and Corporation Finance than  
23 it is being done by Chester's office. I think we may want  
24 them to look at what we find and see if there is any economic  
25 learning to be culled from the data after we have extracted

1 it, but that exercise is, as I say, mostly going on in our  
2 division and at the Office of the Chief Accountant. I  
3 actually this morning just saw their -- Glass Lewis has  
4 identified 142 12B25 filers where the cause of the filing was  
5 inability to complete the 404, the internal control exercise.  
6 And we have actually together with some software services, we  
7 have access to, done a little spreadsheet of what those 142  
8 companies have reported. So there is some stuff going on.  
9 It will continue to go on for the next six weeks or so. My  
10 guess is through the end of April when the 45 day grace  
11 period for the smaller accelerated filers runs out and then  
12 we will look at it. But we are going to use that on an  
13 ongoing basis and I don't have any particular reason to  
14 believe we can't share that purely factual information at  
15 least with you folks.

16 MR. DAVERN: Should we coordinate directly with  
17 you, Alan, or with Mark on the committee, is there a liaison?

18 MR. BELLER: Why don't we start talking through  
19 Jerry at the moment maybe. And Don Nicolaisen, I don't know  
20 if he is sitting behind me or not. You have this habit of  
21 sneaking in, Don. He is going to spend a few minutes with us  
22 and we can maybe talk about who at OCA would be a good  
23 liaison for the committee as well.

24 MR. DAVERN: Okay, thank you.

25 MR. SPATT: And let me just add to what Alan said.

1 One of the special skills that we have in our office is  
2 because of the nature of the backgrounds of our staff with so  
3 many Ph.D.'s in economics, I think our office has very strong  
4 skills with respect to the econo-metric analysis of this type  
5 of data. And I anticipate that we will certainly work  
6 closely with Corporate Finance and the Office of the Chief  
7 Accountant in this sort of context because I think sort of  
8 combining our skills potentially would be quite fruitful.

9 MR. WANDER: Okay, any other questions. If not,  
10 Chester, thank you very much and we look forward to working  
11 with you and your staff.

12 MR. SPATT: Thank you very much for the opportunity  
13 to speak to you this morning.

14 MR. WANDER: And next on our agenda is Don  
15 Nicolaisen, who is the Chief Accountant of the SEC. And I  
16 think many of you met Don yesterday but if you haven't, he is  
17 here to give us an overview of the Office of Chief  
18 Accountant, who is obviously intimately involved in our  
19 issues.

20 MR. NICOLAISEN: Herb, thank you very much and good  
21 afternoon to everybody. I appreciate the opportunity to be  
22 here. We talked about this group for a very long time, and I  
23 have to say I am excited and pleased to see it actually  
24 meeting and discussing the issues. So Alan and I spent many  
25 a night and many a morning and a lot of lunch periods just

1 thinking about what might happen and what we can actually  
2 deal with. So I think we expect great things from this group  
3 and I am sure we won't be disappointed.

4 Let me just speak a little bit about the Office of  
5 Chief Accountant. We are one of the smaller offices within  
6 the Commission. We serve as the advisor to the Commission on  
7 accounting and auditing matters. In that capacity, we are  
8 involved in certain oversight matters involving both the FASB  
9 and the PCAOB. But we also deal with registrants directly  
10 and deal with many of the accounting questions that  
11 registrants have or that their auditors might have.

12 We have ourselves organized into three basic  
13 groups. They are the international side of things, and that  
14 has been an increasing focus for the Commission. It is  
15 certainly an increasing focus for the Office of Chief  
16 Accountant. So for the first time I have a deputy, Julie  
17 Earhardt, who is in charge of that group. Scott Tom is in  
18 charge of accounting matters, those things that deal with  
19 registrants, that would include probably many people in this  
20 room. And Andy Bailey is focused on the auditing end of what  
21 we do, and that includes certain professional standards as  
22 well. Andy, if you want a contact for somebody on 404, Alex,  
23 Andy is probably the right person in our shop. He deals both  
24 with the auditing matters in general but in particular he was  
25 around as Auditing Standard No. 2 was crafted by the PCAOB

1 and passed through the Commission as part of our rulemaking  
2 process.

3           Within my office we also have priorities, and I  
4 might just speak for a minute about a couple of those that  
5 are high on my list. Number one, that I talk about a lot and  
6 I will be continuing to talk about a lot is the need for the  
7 accounting profession and us at the SEC to reduce the level  
8 of complexity that has crept into the accounting world. One  
9 of the most disappointing things that I have to deal with is  
10 to sit down with a registrant and their auditor and they have  
11 come in good faith and they have worked hard and they have  
12 built their case and they have all their research and  
13 homework done. And they say we have recognized revenue and  
14 here is the basis and why we have done what we have done.  
15 And out of the 187 different methods of revenue recognition,  
16 unfortunately I have to tell them you don't have the right  
17 one. You might have done everything right in terms of what  
18 you looked at but you just were in the wrong zip code. That  
19 is not a pleasant thing for anybody to have to deal with, and  
20 I think that when you look at certain areas of our accounting  
21 standards, derivatives, leasing transactions, accounting for  
22 income taxes, some of those basic consolidation practices,  
23 there is an incredible amount of complexity. Much of it has  
24 arisen because of certain interests that want an exception to  
25 the basic rule. And I think as we move forward, we just have

1 to re-think about going back to some basic principles, some  
2 basic concepts in improving the level of financial reporting  
3 by making it simpler. If you embarked on any quality  
4 improvement effort, I think one of the first steps everyone  
5 looks at is what can we take out of the process that is  
6 unnecessary? That is high on my list. Don't expect an  
7 overnight solution but I am also looking for input from this  
8 group as you deal with some of these issues within the  
9 smaller business environs.

10 Another area that we have been working on is  
11 implementation of 123R. Chester talked about that. Chester  
12 and his group have been extremely helpful in the process. I  
13 think we have been able to put out in our SAB-107 certain  
14 short-cuts that should hopefully be helpful to the business  
15 community as you go through implementing stock option  
16 accounting. We have continued to look at certain other  
17 questions and issues. We will continue to do that. And to  
18 the extent that we think we can be helpful in providing  
19 advice in the interest of making this standard work well, we  
20 will be prepared to do that as well.

21 We are also a key player in the 404 Roundtable  
22 tomorrow. It is an initiative that we have been talking  
23 about for many months. It has been on my list of priorities  
24 because we have heard the concerns. Alex had made a  
25 presentation to us from AEA. Others have as well, and we are

1 really interested in hearing those comments. I personally  
2 think that the act itself is fine. It is not particularly  
3 long. I forget what it is, 66 words or something like that.  
4 That section of the act is not particularly complex. I think  
5 most of what we are talking about is the manner in which it  
6 has been implemented. And what we would really hope to do  
7 tomorrow, what I am hopeful that we will hear our, be able to  
8 separate the first time through issues from those things that  
9 are really ongoing. And then to the extent that they are  
10 ongoing things within the application of Section 404 that we  
11 can do something about, we would really like to hear that.  
12 And I know the PCAOB has voiced similar comments and we are  
13 intending to listen. I am very hopeful that we will get some  
14 things that are granular enough for us to really work with.  
15 And that we would be able to move forward with business, the  
16 investor community, the analyst community, and people like  
17 us, regulators, feeling comfortable that we are doing the  
18 right thing in improving the quality of financial reporting.

19 I have a number of other priorities, they may be  
20 slightly less relevant to this group so in the interest of  
21 time I will stop talking at this point other than to do what  
22 is probably most important and that is if you haven't met the  
23 two people from my department who are attached to your group,  
24 I would like to introduce them at this time. It is Alison  
25 Spivey and Jennifer Burns. So with that I am open to any

1 questions that anyone may have.

2 MR. WANDER: Any questions of Don?

3 MR. NICOLAISEN: Burns.

4 MR. WANDER: Okay, Don, thank you so much.

5 MR. NICOLAISEN: That was easy. Good luck to you.

6 As I said, we have high expectations and I am very  
7 enthusiastic about what you are doing. We view small  
8 business as a real growth engine in our economy and we wish  
9 you well. Thank you.

10 MR. BELLER: Thank you, Don. Don, you are going to  
11 have a harder time tomorrow and so am I.

12 MR. WANDER: Putting more lights on down here.

13 MR. BELLER: More light, more heat. If it is okay,  
14 Herb, with you, given that Don just spoke, it is probably  
15 worthwhile to mention to this committee because there is a  
16 coordinated responsibility that I think it is worth you  
17 knowing about on the accounting side. Corporation Finance,  
18 my division, and the division that our Office of Small  
19 Business is attached to, and they will be the people you work  
20 with directly. Also, there are a total of about 540 of us.  
21 So we are one of the larger operations. Over 400 of them  
22 review filings in our disclosure operation section. The  
23 others are organized in a series of support offices. And as  
24 you have questions, we are going to continue to suggest you  
25 work through Jerry and the other designated federal officers

1 who are your subcommittee meetings. But we have resources  
2 behind them in our Office of Chief Counsel, our M&A  
3 operation, international corporate finance and so forth.

4           The one I wanted to mention specifically in light  
5 of you just having heard from Don is the division has its own  
6 Office of Chief Accountant. And I think some of you actually  
7 my chief accountant last night, Carol Stacey. Our Office of  
8 Chief Accountant and frankly our entire review staff works  
9 hand in glove with Don's office in terms of coming up with  
10 appropriate accounting determinations as to what is GAAP and  
11 what is appropriate disclosure. If you look at a formal org  
12 chart of the Commission and a formal list of  
13 responsibilities, Don Nicolaisen's office is the ultimate  
14 arbiter of what is GAAP. And I guess my office and my chief  
15 accountant is the ultimate arbiter of what is good  
16 disclosure. But inevitably when you begin to ask the kinds  
17 of questions that I think you are going to be asking of our  
18 accounting staff, you will end up speaking through I think to  
19 some extent Jerry and his folks but in other cases directly  
20 to Jennifer and Alison and my accountants, really to a  
21 combination of people, and I just wanted to alert you that  
22 there is that sort of coordinated responsibility around here  
23 so that it doesn't throw you the first time you are exposed  
24 to it.

25           MR. WANDER: Okay, thank you. The next item on our

1 agenda is a review of the master schedule and that was  
2 distributed to all of you prior to the meeting. And that  
3 schedule was designed really to sort of lay out from now  
4 until we become sunsetted the various dates. Now this is not  
5 written in stone and it is somewhat fluid. But we thought it  
6 appropriate to give everybody this kind of schedule. You  
7 will notice that it includes six meetings and possible  
8 hearing dates, et cetera. And really if we for our final  
9 recommendations, and this doesn't include any interim  
10 recommendations that we may want to make, we almost have to  
11 be at the research down, pencils writing stage in September,  
12 if not a little bit before then. Because again we are not  
13 all full time and in order to draft something that is of  
14 quality and review it and have the whole committee consider  
15 it, we will need the time from September going forward to do  
16 that.

17           We scheduled meetings about once every other month.  
18 They are on here. If any of you have any great difficulty  
19 with meeting them, would you let us know soon. And if there  
20 is sort of a we can't have hardly anyone attending a  
21 particular meeting, we will give consideration to changing  
22 it. But we all have to recognize that with a group of 20  
23 some people, it is not going to be possible to get everyone  
24 here for every meeting, at least I think that is probably  
25 true.

1           Again, I say this is something that is fluid and  
2   that Jim and I will be on top of. There may be changes as we  
3   go along that are caused by events beyond our control or some  
4   reason that we want to stop or accelerate our process. And I  
5   am open to any comments or suggestions with respect to the  
6   master schedule.

7           MR. DENNIS: Herb, this is Leroy Dennis. One of  
8   the comments that was raised in our subcommittee is whether  
9   the meetings for this committee are always going to be held  
10  here or are we going to try to hold those in other places  
11  around the United States?

12          MR. WANDER: As of right now, we have I guess  
13  reserved this main conference room here in this building and  
14  in the new office. But that doesn't mean we can't have  
15  meetings around the United States and indeed have maybe a day  
16  and a half meeting or two-day meeting and hold hearings with  
17  that. And since you have raised it, Leroy, do you have some  
18  suggestions?

19          MR. DENNIS: No.

20          MR. CONNOLLY: Mr. Chairman, I certainly would  
21  suggest that we consider the two principal cities for  
22  equities trading in this country, equities and their  
23  derivatives, New York and Chicago.

24          MR. WANDER: Okay, we will be happy to do that.  
25  And I would guess if we are going to do that, we would

1 probably want to go visit our brethren out on the West Coast.

2 MR. DENNIS: Yes, we would like that too.

3 MR. WANDER: Would you prefer -- let me ask, Los  
4 Angeles or San Francisco?

5 MR. DENNIS: San Francisco.

6 MR. WANDER: Since my two daughters live there,  
7 that is easy.

8 MR. BELLER: Steve is ready for Palo Alto.

9 MR. DENNIS: I think the real question is would we  
10 get benefit by being out on location and would that allow  
11 additional input that we may not get if we just stay here in  
12 Washington.

13 MR. WANDER: I do think that is probably true. So  
14 let Jim and I take that under very serious consideration and  
15 we will do that right away so we can plan things far enough  
16 in advance.

17 MS. DOLAN: Mr. Chairman, I have a question for  
18 Alan Beller, which is what is the likely timeline to come out  
19 of the effort tomorrow? Are you anticipating that we will  
20 have a parallel timeline here where you are going to have  
21 recommendations that may be impacting all companies?

22 MR. BELLER: I think to some extent the timelines  
23 will be parallel, but I think that given the fact that the  
24 2005 audit cycle, and I guess Don didn't stay behind, I am  
25 not going to put words in his mouth, but I think he agrees

1 with this, given that the 2005 audit cycle is really actually  
2 almost begun for calendar year companies, I think we think  
3 that a first cut of guidance to the extent we conclude that  
4 we can do something by way of interpretative help or help by  
5 way of guidance, either at the Commission staff level, or and  
6 I am about to put words in Dan's mouth as well, at the PCOAB  
7 staff level, I think we would seek to encourage that to  
8 happen frankly in the next like six weeks. That is not a  
9 promise but I think it is an objective. I think if we go  
10 much beyond that, it will begin to have less applicability.  
11 That is a first cut. I think there will be a lot of things  
12 that remain unaddressed and undigested from the roundtable  
13 and from the comments after that period. And I would expect  
14 that we would follow -- at that point, we would be following  
15 a parallel timeline with this committee with respect to what  
16 remains. But I think you should expect us to try to do a  
17 first round probably before this committee really can get  
18 much of anything in front of us. And from your point of  
19 view, I wouldn't be worried about that. As I say, I think it  
20 is a first round of sort of the obvious things that we think  
21 we can address on an interpretive basis.

22           An example of something, I am not going to  
23 pre-judge what we are going to do, if anything, but I think  
24 an example of the kind of thing that we would try to look at  
25 relatively quickly would be the relationship between

1 companies and auditors and whether it is has become  
2 appropriately arms length, whether it has become too arms  
3 length, whether there is anything that can be provided by way  
4 of guidance on that that would at one and the same time  
5 preserve auditor independence, preserve the ability of  
6 auditors to make appropriate assessments of internal control,  
7 but yet allow companies to have an appropriate level of  
8 dialogue and consultation with their professional advisors.  
9 That is the kind of thing that I think if there is a way to  
10 address it quickly, we will try to address it quickly. But  
11 that leaves, as I say, there is going to be a ton of things  
12 that come out of the roundtable and they are in the comment  
13 file already that we will be working on for several months I  
14 expect.

15 Dan, I don't know if you have a different view.

16 MR. GOELZER: No, I think we would say exactly the  
17 same things. I think we know already that there are a number  
18 of interpretive or implementation issues that we can possibly  
19 address just from the comment letters and from reactions we  
20 have gotten from people and other sources. And if that stuff  
21 is going to have any impact on the next audit cycle, we need  
22 to get something out in 30 days, six weeks, 60 days,  
23 something in that near term kind of time range. To the  
24 extent there might be further rulemaking, new standards,  
25 amendments to the existing standards, that would be on a

1 longer term.

2 MR. BROUNSTEIN: A question, just as a follow-up,  
3 Rick Brounstein. Is there a listing of that somewhere?  
4 Because a lot of the things that you are throwing out are  
5 things that maybe cover big companies as well as little  
6 companies. And I know in our subcommittee we have been kind  
7 of wrestling with a lot of those and maybe we should be  
8 focusing on other topics if they are already going to be  
9 handled at this level?

10 MR. BELLER: The answer is that we don't, at least  
11 I don't have a list of any formal sort. I carry around a  
12 list in my head and it is going to inform the questions I ask  
13 at the roundtable tomorrow and I am moderating it. But I  
14 think that is a list that is going to become apparent in the  
15 next somewhere between 30 and 60 days.

16 MR. WANDER: Alan, is there or are you going to do  
17 a summary of the comment letters you have received for the  
18 roundtable?

19 MR. BELLER: I honestly don't know the answer to  
20 that question. I assume the predicate for your question is  
21 that when we do a rulemaking, we generally provide, we do  
22 prepare a summary of the comments that are received in the  
23 comment file for those rules. And that is publicly  
24 available. We are not in a rulemaking mode and so I honestly  
25 don't know what we are going to do in that regard. I can try

1 to find out whether we are going to do that or not. It would  
2 obviously be of use to you guys and it would probably be of  
3 use to us as well.

4 MR. WANDER: And is there any plan to have, I know  
5 this is hard, a summary of the hearings tomorrow?

6 MR. BELLER: I don't think we have generally done  
7 that. The transcript will be available and the hearings will  
8 continue to be available or the roundtable will continue to  
9 be available on our web site. Let me ask Jennifer, she has  
10 escaped too? Alison, do you have any idea whether we plan to  
11 do that? My guess is that we don't, Herb.

12 MS. SPIVEY: I have not heard anything.

13 MR. WANDER: Well, Jim and I both plan to attend  
14 tomorrow so I will try and (a) stay awake; and (b) take good  
15 notes, and (c) get them to you. So at least my perception of  
16 what the high points are and where I guess there -- I will  
17 also try and sort of where there seems to be agreement, we  
18 will let you know that and where there seems to be  
19 disagreement, we will let you know that. So we will have our  
20 own internal sort of summary system. There are how many, 120  
21 letters then, comments or something like that?

22 MR. BELLER: I think it is like 185 or 186.

23 MR. WANDER: Well, if it was summer associate time  
24 I could have somebody summarize this for us but I guess we  
25 will have to wait until summer associates come to work.

1           MR. CONNOLLY: Mr. Chairman, along those lines, may  
2 I ask Mr. Beller another question? We have had  
3 presentations, largely from your good self as a division,  
4 from the chief accountant and the chief economist, I can't  
5 help but notice that the Division of Enforcement is  
6 conspicuous by their absence. And given the impact of  
7 capital formation and the bright lines that are necessary to  
8 fall within those parameters and also the concerns and the  
9 problems, the enforcement problems the Commission has had,  
10 having to do with excesses or violations in that formation  
11 process, do you think it is possible we could have some  
12 discussion or some inputs from that division to help inform  
13 our recommendations?

14           MR. BELLER: I suppose my answer to that would be I  
15 think we could arrange that. I actually think, not because  
16 they wouldn't try to be helpful, but because of the nature of  
17 the enforcement process and the nature of the fact that it is  
18 unlike rulemaking and unlike interpretation, each enforcement  
19 case walks in on its own four feet and walks out on its own  
20 four feet and generalization is difficult. So I am not sure  
21 frankly what the committee would get out of that. I think if  
22 you had specific questions about our enforcement policy and  
23 the micro-cap or the small cap or the capital formation area,  
24 we can try to provide you some answers. I am not sure a  
25 general presentation would tell you very much.

1           MR. CONNOLLY: Appreciate it.

2           MR. CLOUTIER: Mr. Chairman, Rusty Cloutier. Alan,  
3 there was a very good letter handed to us this morning, and I  
4 think it stated it very well from a Mr. Dennis Valentine that  
5 was handed to all the committee members this morning talking  
6 about our timetable and the timetable for non-accelerated  
7 filers. And the difficulty of a company that is somewhat  
8 close to \$75 million and that the rules may change, as we  
9 said writing in September and their having to make some  
10 decisions in June, if you all when you would have an  
11 opportunity if you all could review that. I know Kevin  
12 apparently just got it this morning and just maybe give a  
13 response to the committee as to some of your thoughts on  
14 that. It is a very interesting letter, very well-written,  
15 and since I am almost in the same situation, it raised a lot  
16 of thoughts I had in my own mind.

17           MR. WANDER: Yes, I will be happy to do that. I  
18 looked at it relatively quickly. I actually think we can  
19 address most of this wherever your recommendations go and  
20 whatever our rules ultimately turn out to be by being  
21 somewhat sensible in our transition provisions. But we will  
22 look at it and tell the committee what we think.

23           The only other point I would make about the \$75  
24 million, and I didn't make it when Steve Bochner was talking  
25 about it, but since you have given me another opportunity, I

1 will. And I think really all it is is a further  
2 reinforcement of something that several folks on the  
3 committee have already said today, which is that the work of  
4 your various subcommittees is to some extent intertwined and  
5 interrelated. The \$75 million accelerated filer category,  
6 which Steve identified as, gee, maybe a little small for  
7 certain purposes, is also today the cut off for shelf  
8 registration, which means delayed offerings, immediate access  
9 to the markets and so on and so forth. And I think it is  
10 incumbent on this committee to think about from the capital  
11 formation point of view what you want to do with that \$75  
12 million number if you are going to move it for disclosure  
13 purposes. That is the only thing I will say but that it is  
14 that kind of thing that demonstrates the interaction between  
15 the two. And I guess I had somewhat that reaction to Mr.  
16 Valentine's letter as well. I think it raises a lot of good  
17 points. I also think it cuts both ways. And I think we all  
18 have to be mindful of that.

19 MR. WANDER: I will save my comments on size. It  
20 is a delicate issue but I think we are off to actually a good  
21 start. I think we have a number of good ideas that we, at  
22 least in one or two of the subcommittees, that we want to  
23 pursue that make to me a lot of sense initially. I can  
24 always be proven wrong. But that may be very good.

25 If there are no other comments on the schedule, we

1 will move into item eight on the agenda, which is really  
2 after our long discussion this morning, and I think very  
3 fruitful discussion, about our summary agenda that will be  
4 published as soon as we include those items we added this  
5 morning. Is there any other discussion before we adopt that  
6 so that it can be circulated outside this group to ask for  
7 comment? If there are none, I will entertain a motion to  
8 approve the summary agenda as revised this morning.

9 MR. CONNOLLY: So move the adoption of the summary  
10 agenda.

11 MR. WANDER: Is there a second?

12 MS. DOLAN: Seconded, Mr. Chairman.

13 MR. WANDER: Thank you. Any further discussion?  
14 If not, all in favor aye.

15 [Chorus of ayes.]

16 MR. WANDER: Opposed? Abstentions? So it is  
17 passed unanimously.

18 And now we are actually an hour early and we are at  
19 discussion of next steps. And I don't want to keep you all  
20 here longer than expected. A good chairperson always gets  
21 the meeting done early. One of the next steps, I wrote down  
22 I guess a couple of things that we have to, that Jim and I  
23 have to do is figure out a process to bring the whole  
24 committee into a discussion of this size question. Secondly,  
25 we have to work on a meeting schedule that might include some

1 meetings outside of Washington, D.C. And, third, develop a  
2 process so that we have an effective way of dealing with the  
3 resources here at the Commission, and particularly the Office  
4 of Economic Analysis, which we will let each subcommittee  
5 know how to handle. The next item will be that I know all  
6 the subcommittees have scheduled meetings, and I think as  
7 soon as those first meetings are over or before those first  
8 meetings, Jim and I will be in contact with the subcommittee  
9 chairs to start our own analysis. And I think we started  
10 really running right on start. We are not turtles at the  
11 beginning of the race here. Everybody was at the starting  
12 line and we are off and running. So I am very complimentary  
13 of everybody for being well prepared here and being energetic  
14 about attacking this schedule. But I don't think there are  
15 any other items on the agenda other than anything anyone  
16 wants to raise. Yes, Alan?

17 MR. BELLER: I just want to follow-up, Herb, on  
18 your to-do list. I think two thoughts for you on maybe what  
19 our to-do list should be without waiting for further requests  
20 and suggestions. One is to figure out, and I guess they both  
21 relate in some sense in the first instance to the work of the  
22 internal control subcommittee, though I think they could  
23 ultimately have broader application. One is to try to figure  
24 out to the extent there is work done here that is not sort of  
25 still private and deliberative but things like summaries of

1 the comment letters and so forth that we could share with you  
2 folks, figuring out what that is likely to be and whether we  
3 can do it or not. I am not committing because I don't quite  
4 know myself what the ground rules are but let me see what  
5 there is. And perhaps at least some directional advice as to  
6 what we are looking at as we go along so that you don't look  
7 at some things where we think we are going to do something  
8 relatively quickly.

9           The other would be if you look at the public --  
10 again, in the first instance for internal control but it may  
11 have broader applicability, to the extent you look at the  
12 public comment file that we have opened and to the extent you  
13 look elsewhere around, there are a lot of organizations which  
14 have done surveys, questionnaires and so forth. FEI has done  
15 I think three or four surveys now on the cost of internal  
16 control and the benefits. The NASDAQ recently submitted to  
17 the comment file a summary of a questionnaire and the  
18 responses that they have received. We can maybe try to  
19 figure out what of those we know that is publicly available  
20 through a combination of Corporation Finance and OCA. But I  
21 think I would be very surprised if those organizations who  
22 certainly are interested in meeting with us from time to time  
23 to share their conclusions that they have obtained, I would  
24 have thought that various subcommittees might want to also  
25 sit down with those folks and hear firsthand as opposed to

1 through us what their views might be and let us get together  
2 as I say that list of who has done these publicly available  
3 studies and share that with you as well.

4 MR. WANDER: That is a good idea, good idea. Are  
5 there any other items of business that any of the members  
6 would like --

7 MR. ROYSTER: Mr. Chairman, Scott Royster. My  
8 apologies if I have missed this but in order for us to  
9 communicate with each other, is there a contact list that  
10 might include phone numbers and email addresses so that  
11 either individually or from a group perspective we can  
12 communicate outside of these meetings?

13 MR. WANDER: Yes, and we will get you one this  
14 afternoon.

15 MR. ROYSTER: Thank you.

16 MR. WANDER: John?

17 MR. VEIHMEYER: John Veihmeyer, just to clarify the  
18 discussion on future meeting dates and locations. To the  
19 extent we want to move it to different locations, I assume  
20 that would be to have some type of public outreach in  
21 connection with that. So should we assume that the dates  
22 currently on our schedule may be expanded by a day? In other  
23 words, it looks like one-day meetings that are scheduled. To  
24 the extent you are contemplating moving them around, it seems  
25 like the only value in doing that would be if we had some

1 kind of outreach otherwise we could just continue to meet in  
2 Washington. So is that something you will get back to us on  
3 and let us know but at this point we need to be conscious of  
4 the fact that some of those one-day meetings may expand into  
5 a day and a half or two day meetings?

6 MR. WANDER: I think so. I think it is a good  
7 point, yes. And that is one of the reasons I put it as a  
8 high priority to get back to you as quickly as possible. I  
9 think the master schedule actually says and hold possible  
10 hearings on it. I have done some of these things in a day.  
11 We might want to start a meeting at 8:00 in the morning and  
12 go to noon, take an hour break and then go from like 1:00 to  
13 5:00 with hearings. So it can be done because I know how  
14 valuable everybody's time is. Alan?

15 MR. BELLER: I am sorry, I just want to interrupt  
16 for one more moment. Commissioner Goldschmid has joined us  
17 and you did not have an opportunity to meet him last evening  
18 or earlier today, so I just wanted to let the committee  
19 members know that Harvey Goldschmid, another of our  
20 commissioners who is very enthusiastic and supportive of this  
21 committee's work has joined us this afternoon. So thank you.

22 MR. WANDER: Harvey, would you care to say a few  
23 words?

24 COMMISSIONER GOLDSCHMID: We are all delighted you  
25 are here and you are doing what you are doing. I was shocked

1 to hear you talking about 404 when I came in. Anyway, I  
2 think it is terrific that you are all here. It is a terrific  
3 group from what I have seen in terms of your resumes and all  
4 of you coming together, and I am very much looking forward to  
5 seeing what you accomplish. Thank you.

6 MR. WANDER: Thank you. With that send off, is  
7 there a motion for adjournment?

8 MR. CONNOLLY: So moved.

9 MR. WANDER: A second?

10 MR. JAFFEE: Second.

11 MR. WANDER: All in favor?

12 [Chorus of ayes.]

13 MR. WANDER: Opposed? Thank you all.

14 (Whereupon, the SEC Advisory Committee on Smaller  
15 Public Companies was adjourned at 2:37 p.m.)

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*Comm 3/11/05*  
*7/9/05*

Securities and Exchange Commission  
Advisory Committee on Smaller Public Companies

1. By-Laws and Operating Procedures

(As adopted on April 12, 2005)

The following By-Laws and Operating Procedures (“By-Laws”) will govern the operations of the Securities and Exchange Commission Advisory Committee on Smaller Public Companies (the “Committee”).

**Section I: Purpose, Organization and Operation**

The purpose of the Committee is to assist the U.S. Securities and Exchange Commission (the “Commission”) in assessing the current securities regulatory system in the United States relating to disclosure, financial reporting, internal controls and offering exemptions for smaller companies, and to make recommendations for changes. The Committee has been formed under the Federal Advisory Committee Act, 5 U.S.C.–App. 1 (“FACA”), which governs the creation and operation of advisory committees by federal government agencies, by the filing of its Charter on March 23, 2005 with the Committee on Banking, Housing, and Urban Affairs of the United States Senate and the Committee on Financial Services of the U.S. House of Representatives. Notwithstanding anything to the contrary in these By-Laws, the Committee will operate in accordance with FACA and its implementing regulations, and with its Charter, as the same may be amended from time to time.

**Section II: Members and Official Observers**

The Members of the Committee are appointed by and serve at the pleasure of the Chairman of the Commission as may be appropriate for the accomplishment of the Committee’s purposes and in order to balance the viewpoints required to effectively address those purposes. Official Observers are invited by the Chairman to serve as official observers of the Committee; they also serve at the pleasure of the Chairman. Official Observers have all rights of Members of the Committee except the right to vote or to make a motion for a vote.

**Section III: Meetings**

**(A) In General.** The Committee will meet at such intervals as are necessary to carry out its duties. Meetings may be called by the Co-Chairs of the Committee with the approval of the Designated Federal Officer of the Committee appointed in accordance with FACA (“DFO”), or by the DFO. One of the Co-Chairs of the Committee will preside at all meetings of the Committee, unless the Chairman of the Commission directs the DFO to preside in accordance with FACA. The presiding officer may specify the use of rules of parliamentary procedure consistent with these By-Laws. Subject to such reasonable guidelines and procedures as the presiding officer or the Committee may adopt, Members and Official Observers may participate in a meeting by means of conference telephone or similar communications equipment if all Members and Official Observers can hear one another at the same time and members of the public entitled to hear them can do so.

**(B) Notice.** The Committee will publish a notice of each meeting in the *Federal Register* at least 15 calendar days before the meeting. The notice will include (1) the name of the Committee; (2) the time, date, place and purpose of the meeting; (3) a copy or summary of the agenda; (4) a statement as to whether all or part of the meeting will be open to the public and, if any part is closed, a statement as to why, citing the specific statutory provisions that serve as the basis for closure; (5) any notice required by Section III(F) if oral public comment is to be excluded; and (6) the name and telephone number of the DFO or other Commission official who may be contacted for additional information concerning the meeting.

**(C) Agenda.** The Co-Chairs will adopt an agenda for each meeting of the Committee sufficiently in advance of the meeting to permit a copy or summary of the agenda to be published with the notice of the meeting. The DFO must approve the agenda before such publication. The Commission staff will distribute the agenda to the Members and Official Observers before each meeting. Items for the agenda may be submitted to the Co-Chairs through the DFO by any Member or Official Observer of the Committee or by any member of the public.

**(D) Voting.** A Member must be participating in a meeting personally to cast a vote. When a decision or recommendation of the Committee is required, the presiding officer will request a motion for a vote. Any Member may make a motion for a vote and vote. No second after a proper motion will be required to bring any issue or recommendation to vote. Committee action based on a vote requires a simple majority of the votes cast at a meeting at which there is a quorum.

**(E) Quorum.** A quorum will consist of a simple majority of the Members, not including Official Observers.

**(F) Open Meetings.** Unless otherwise determined in advance, all meetings of the Committee will be open to the public. Once an open meeting has begun, it may not be closed for any reason. If, during the course of an open meeting, matter inappropriate for public disclosure arises during discussion, the presiding officer will order such discussion to cease and will schedule it for closed session. All materials brought before, or presented to, the Committee during an open meeting will be available to the public for review or copying at the time scheduled for the meeting. All such materials also will be available on the Committee's web site before the meeting or added to the web site as soon as practicable afterwards. The Co-Chairs may decide in advance to exclude oral public comment during a meeting, in which case the meeting announcement published in the *Federal Register* will note that oral comment from the public will not be permitted and will invite written comment as an alternative. Members of the public may submit written statements to the Committee at any time.

**(G) Closed Meetings.** All or parts of meetings of the Committee may be closed in limited circumstances in accordance with applicable law. Requests for closed meetings must be submitted by the DFO to the Chairman of the Commission under FACA, generally at least 30 days in advance of the meeting. The appropriate Commission official must determine that closing the meeting is consistent with the provisions of the Government in the Sunshine Act. Consistent with Section III(B)(4), the notice of the closed meeting published in *Federal Register* must include information on the closure.

**(H) Hearings.** The Committee may hold hearings to receive testimony or oral comments, recommendations and expressions of concern from the public. The Committee may hold hearings at open meetings or in closed session in accordance with the standards in these By-Laws for closing meetings to the public. The Co-Chairs or the Committee may specify reasonable guidelines and procedures for conducting orderly and efficient hearings, such as requirements for submitting requests to testify and written testimony in advance and placing limitations on the number of persons who may testify and the duration of their testimony.

**(I) Minutes.** The DFO will prepare minutes of each meeting of the Committee and submit them to the Co-Chairs for certification of their accuracy. At least one Co-Chair must certify as to the accuracy of the minutes. The DFO will distribute copies of the certified minutes to each Member and Official Observer. Minutes of open meetings will be available to the public on the Committee's web site. Minutes of closed meetings will also be available to the public upon request, subject to the withholding of matters about which public disclosure would be harmful to the interests of the Government, industry, or others, and which are exempt from disclosure under the Freedom of Information Act. The minutes will include a record of persons present (including the names of Committee Members and Official Observers, names of Commission staff providing support services to the Committee, and names of members of the public who made written or oral presentations); a complete and accurate description of the matters discussed and conclusions reached; and copies of all reports received, issued or approved by the Committee.

#### **Section IV: Officials**

**(A) Co-Chairs.** The Co-Chairs of the Committee are appointed by and serve at the pleasure of the Chairman of the Commission to perform the duties specified in these By-Laws. The Co-Chairs will work with the DFO to establish priorities, identify issues that should be addressed, determine the level and types of staff and financial support required and serve as the focal point for the Committee's membership.

**(B) Designated Federal Officer.** The DFO is designated by the Chairman of the Commission and serves as the Federal Government's agent for matters related to the Committee's activities. By law, the DFO must, among other things, approve or call all meetings of the Committee, approve agendas, attend all meetings, and adjourn meetings when such adjournment is in the public interest. In addition, the DFO is responsible for providing adequate staff support to the Committee, including staff to assist the DFO in the performance of the following functions: (1) notifying Members and Official Observers of the time and place for each meeting; (2) maintaining records of all meetings, including subcommittee meetings, as required by law; (3) maintaining the roll; (4) preparing the minutes of all meetings of the Committee and its subcommittees; (5) attending to official correspondence; (6) maintaining official Committee records, including subcommittee records; (7) maintaining a web site for the Committee; (8) acting as the Committee's agent to collect, validate and pay all vouchers for pre-approved expenditures; and (9) preparing and handling all reports, including the annual report of the Committee required by FACA.

**(C) Support Staff.** The Chairman of the Commission has agreed that staff from the Commission's Division of Corporation Finance, and in particular the

Division's Office of Small Business Policy, will be available to the DFO to provide adequate staff support for the Committee.

#### **Section V: Subcommittees**

The Co-Chairs of the Committee, with the approval of the DFO, may convene subcommittees to support the Committee's functions and may appoint Members and Official Observers to, and Chairs of, any subcommittees so convened. The Co-Chairs will be *ex officio* members of all subcommittees. Only Members of the Committee will have the right to vote and make a motion for a vote in a subcommittee. No subcommittee will have any authority to provide advice or recommendations (1) directly to the Commission or (2) to be adopted by the Committee without discussion or consideration at an open meeting of the Committee. All activities of the subcommittees will be in compliance with FACA.

#### **Section VI: Records**

All documents, reports and other materials prepared by or submitted to the Committee constitute official governmental records and must be maintained in accordance with FACA's policies and procedures.

#### **Section VII: Expenses**

Expenses related to the operation of the Committee will be borne by the Commission. Expenditures of any kind must be approved in advance by the DFO.

#### **Section VIII: Amendments**

These By-Laws may be amended from time to time by vote of the Members.

Exhibit B

As Approved for Public Comment on April 12, 2005

**Summary of Committee Agenda**

1. Definition of “Smaller Public Company.”
  - 1.1. Develop preliminary observations to be used for analysis of each substantive area under items 2 through 7 below.
  - 1.2. Examine appropriateness of existing definitions.
  - 1.3. How do existing definitions work? Are they meaningful and effective? Are they practical? Is it possible to develop risk-based or other definitions? Seek economic analysis.
2. Internal Control – Section 404 of Sarbanes-Oxley; S-K Item 308, S-X Reg. § 210.2-02(e).
  - 2.1. Evaluate first quarter 2005 reports.
    - 2.1.1. Effective control.
      - \* Size/characteristics of company.
    - 2.1.2. Ineffective control.
      - \* Size/characteristics of company.
      - \* Reasons for failure.
      - \* Materiality of failure.
  - 2.2. Evaluate benefits and costs/burdens for smaller public companies, including disproportionate costs/burdens, competitive disadvantages and effectiveness in preventing fraud.

- 2.2.1. Seek economic input.
  - 2.2.2. Consider impact on “tone at the top.”
  - 2.2.3. Versus private companies and foreign companies.
- 2.3. Evaluate procedures used in first quarter reports.
  - 2.3.1. Company procedures.
  - 2.3.2. Auditor procedures.
  - 2.3.3. What worked well.
  - 2.3.4. What worked less well or did not work.
- 2.4. Mechanisms to evaluate.
  - 2.4.1. Questionnaires prepared by FEI, NASDAQ and others.
  - 2.4.2. One or more roundtables held by SEC and PCAOB.
  - 2.4.3. Other written or oral input.
- 3. Corporate Governance Standards.
  - 3.1. Review and catalog.
  - 3.2. Evaluate impact of requiring independent directors for smaller public companies.
    - 3.2.1. Boards themselves and Committees.
    - 3.2.2. Impact on controlling families or other controlling shareholders.
    - 3.2.3. Impact on other stakeholders.
    - 3.2.4. Impact of stakeholders on effectiveness of independent directors.
    - 3.2.5. Loss of market and company knowledge and experience.

- 3.3. Evaluate impact of independence definitions.
  - 3.3.1. Boards themselves and Committee.
  - 3.3.2. Adequate supply of competent directors.
  - 3.3.3. How are boards/committees performing?
  - 3.3.4. Cost of board operation.
  - 3.3.5. Other.
- 3.4. Evaluate impact of special requirements on audit committee make-up and operation.
  - 3.4.1. Special independence requirements.
  - 3.4.2. Financial expertise requirements and disclosure requirements.
  - 3.4.3. Loss of operational knowledge, experience and depth.
- 3.5. Recommendations.
- 4. Effects of other Statutory Requirements and Commission Regulations, including under Sarbanes-Oxley, on Smaller Public Companies.
  - 4.1. Officers' certifications.
  - 4.2. Auditing firm's standards and requirements.
  - 4.3. Prohibition of loans to executive officers and directors.
  - 4.4. Other.
  - 4.5. Recommendations.
- 5. Disclosure Requirements.

- 5.1. How do disclosure requirements affect smaller public companies?
- 5.2. Analyze Regulation S-B (including seeking economic input).
- 5.3. Analyze forms and requirements.
  - 5.3.1. Exchange Act periodic reporting forms (10-K, 10-KSB, 10-Q, 10-QSB).
  - 5.3.2. Special Securities Act forms (SB-1, SB-2).
  - 5.3.3. Are S-B forms helpful, beneficial, effective or negative, both for the issuer and the investor market?
- 5.4. Identify other aspects of disclosure regime that might be modified for smaller public companies.
- 5.5. Identify other possible scaling standards.
  - 5.5.1. Is size the most appropriate standard or is risk?
  - 5.5.2. Are revenues a better scaling standard for some disclosure rules and other regulations?
  - 5.5.3. Should other alternatives be considered?
- 5.6. Liability concerns.
- 5.7. Consider issues of delinquent and deficient micro-cap disclosure.
- 5.8. Evaluate the balance of disclosure to protect investors with the competitive needs of smaller public companies.
- 5.9. Recommendations.
6. Accounting Principles.
  - 6.1. Evaluate “one size fits all” vs. “Big GAAP-Little GAAP.”

- 6.2. Identify priority accounting principles, if any, where modifications might be considered for smaller public companies.
- 6.3. Emphasize importance of cash in many smaller companies.
- 6.4. Analyze overlay and impact of other regulatory schemes (financial institutions, insurance, government contractors, etc.).
- 6.5. Analyze role of outside audit firms with respect to smaller companies, e.g., environmental shift in role of auditors, communications with outside auditors, concentration of Big Four accounting firms, difficulty in switching audit firms.
- 6.6. Analyze whether extended effective dates for smaller companies are appropriate for future accounting principles.
- 6.7. Recommend changes, if any.
7. Capital Formation.
  - 7.1. Analyze existing structure.
  - 7.2. Analyze selected exemptions from registration and subsequent reporting.
  - 7.3. Evaluate Regulation A.
  - 7.4. Analyze investment banker roles.
  - 7.5. Analyze analysts' coverage.
  - 7.6. Costs and timing to get access to markets.
    - 7.6.1. Broader access to capital, including foreign markets.
    - 7.6.2. Possible roles of capital formation specialists, including brokers and "finders."

7.7. Cost of and ability to exit the markets.

7.8. Possible improvements in interaction and interplay between federal law or SEC, state laws or state regulators, and self-regulatory organizations and rules (e.g., Rule 15c2-11).

7.9. Liability issues.

7.10 Recommendations.

8. Small Business Forums and Related Issues.

8.1. Analyze recommendations from recent SEC Small Business Forums.

8.2. Review small business statutes (Regulatory Flexibility Act and 1980 Small Business Investment Incentive Act).

## SEC Advisory Committee on Smaller Public Companies

### Committee Agenda

The following overarching principles should characterize the Committee's work:

- Further Commission's Investor Protection Mandate.
- Seek Cost Choice/Benefit Inputs.
- Keep It Simple.
- Maintain Culture of Entrepreneurship.
- Capital Formation Should Be Encouraged.
- Recommendations Should Be Prioritized.

#### 1. Definition of "Smaller Public Company."

1.1 Develop preliminary observations to be used for analysis of each substantive area under Items 2 through 7 below.

1.2 Examine appropriateness of existing definitions.

1.2.1 Small business ("S-B") issuer -- less than \$25 million in public float and revenues.

1.2.2 Accelerated filer definition – more than \$75 million in market float.

1.2.3 Fewer than 500 shareholders of record and \$10 million in assets (Exchange Act §12(g) standard, including implications of issuing employee stock options).

1.2.4 Use of Registration Statement S-3.

1.2.5 Well-known seasoned issuers (public float of at least \$700 million by non-affiliates).

1.2.5 Listing standards.

\* NYSE.

- \* NASDAQ.
- \* AMEX.
- \* OTCBB.
- \* Pink Sheets.
- \* Others.

1.2.6 Market definitions of “small cap” and “micro cap.”

1.2.7 Other definitions?

1.3 How do existing definitions work? Are they meaningful and effective? Are they practical? Is it possible to develop risk-based or other definitions? Seek economic analysis.

1.4 Utilize the SEC Office of Economic Analysis to evaluate the definitions.

2. Internal Control – Section 404 of Sarbanes-Oxley; S-K, Item 308, S-X, Reg ¶210.2-02(e).

2.1 Evaluate first quarter 2005 reports.

2.1.1 Effective control.

- \* Size/characteristics of company.

2.1.2 Ineffective control.

- \* Size/characteristics of company.
- \* Reasons for failure.
- \* Materiality of failure.

2.2 Evaluate benefits and costs/burdens for smaller companies, including disproportionate costs/burdens, competitive disadvantages and effectiveness in preventing fraud.

2.2.1 Seek economic input.

2.2.2 Consider impact on “tone at the top.”

2.2.3 Versus private companies and foreign companies.

- 2.2.4 Evaluate cost choices imposed on companies.
- 2.2.5 Evaluate the leadership mindshare shift required.
- 2.2.6 Evaluate potential diminishing returns to investors.
- 2.2.7 Estimate annual cost of being public relative to profit potential.

2.3 Evaluate procedures used in first quarter reports.

- 2.3.1 Company procedures.
- 2.3.2 Auditor procedures.
- 2.3.3 What worked well.
- 2.3.4 What worked less well or didn't work.

2.4 Mechanisms to evaluate.

- 2.4.1 Questionnaires prepared by FEI, NASDAQ and others.
- 2.4.2 One or more roundtables held by SEC and PCAOB.
- 2.4.3 Other written or oral input.
  - \* Define "tone at the top."
  - \* Seek information re: costs and benefits.

2.5 Based on evaluation, recommend or support modifications, if any, to:

- 2.5.1 SEC regulations.
- 2.5.2 PCAOB Auditing Standard No. 2.
- 2.5.3 COSO (including evaluation of task force proposal).
- 2.5.4 Recommend or support delaying effectiveness for non-accelerated filers or others.
- 2.5.5 Consider staggering reports – i.e., a report might be due every other year rather than every year.
- 2.5.6 Other alternatives.

3. Corporate Governance Standards.

- 3.1 Review and catalog.
  - 3.1.1 NYSE.
  - 3.1.2 NASDAQ.
  - 3.1.3 Other (AMEX, OTCBB, Pink Sheets).
  - 3.1.4 Private entities.
    - \* Ratings and standards: ISS, Corporate Library, IRR, Moody's, etc.
    - \* Institutional standards: CALPERs, TIAA-CREFF, others.
- 3.2 Evaluate impact of requiring independent directors for smaller companies.
  - 3.2.1 Boards themselves and Committees.
  - 3.2.2 Impact on controlling families or other controlling shareholders.
  - 3.2.3 Impact on other stakeholders.
  - 3.2.4 Impact of stakeholders on effectiveness of independent directors.
  - 3.2.5 Loss of market and company knowledge and experience.
- 3.3 Evaluate impact of independence definitions.
  - 3.3.1 Boards themselves and Committees.
  - 3.3.2 Adequate supply of competent directors.
  - 3.3.3 How are boards/committees performing?
  - 3.3.4 Cost of board operation.
  - 3.3.5 Other.
- 3.4 Evaluate impact of special requirements on audit committee make-up and operation.

- 3.4.1 Special independence requirements.
  - 3.4.2 Financial expertise requirements and disclosure requirements.
  - 3.4.3 Loss of operational knowledge, experience and depth.
- 3.5 Evaluate impact of stockholder approval of equity compensation plans.
- 3.6 Recommendations.
- 4. Effects of other Statutory Requirements and Commission Regulations, including under Sarbanes-Oxley, on Smaller Businesses.
  - 4.1 Officers' certifications.
  - 4.2 Auditing firm's standards and requirements.
    - 4.2.1 Independence.
    - 4.2.2 Partner rotation.
    - 4.2.3 See above re: internal control audit.
  - 4.3 Prohibition of loans to executive officers and directors.
  - 4.4 Other.
    - 4.4.1 Whistleblower regulation.
    - 4.4.2 Reg. G.
    - 4.4.3 Accelerated filing deadlines.
    - 4.4.4 Increased SEC review of periodic reports.
    - 4.4.5 Codes of conduct.
    - 4.4.6 Disgorgement for restatements.
    - 4.4.7 Benefit plan blackouts.
    - 4.4.8 Officer and director bars.
    - 4.4.9 Increased criminal sanctions.
  - 4.5 Recommendations.

5. Disclosure Requirements.

- 5.1 How do disclosure requirements affect smaller public companies?
- 5.2 Analyze Regulation S-B (including seeking economic input).
  - 5.2.1 Is size definition of S-B correct?
  - 5.2.2 Irrespective of the size of issuer, is Regulation S-B helpful, effective or beneficial?
  - 5.2.3 What is the market reaction to S-B companies?
  - 5.2.4 What changes, if any, to improve or replace S-B?
- 5.3. Analyze forms and requirements.
  - 5.3.1 Periodic reporting Exchange Act forms (10-K, 10-KSB, 10-Q, 10-QSB).
  - 5.3.2 Special Securities Act forms (SB-1, SB-2).
  - 5.3.3 Are S-B forms helpful, beneficial, effective or negative, both for the issuer and the investor market?
  - 5.3.4 What is the market reaction to S-B forms?
  - 5.3.5 What changes, if any, to recommend?
    - \* Modified quarterly reporting (perhaps only revenue and ownership information and brief MD&A)?
    - \* Semi-annual instead of quarterly periodic reporting?
    - \* Permitting “fully comply” certification to be affixed to incomplete filings, with appropriate disclosure, instead of withholding information from investors until filing is complete?
- 5.4 Identify other aspects of disclosure regime that might be modified for smaller companies.
  - 5.4.1 MD&A.

- 5.4.2 Proxy rules (14A and C).
- 5.4.3 Williams Act (13D and G).
- 5.4.4 Regulation FD.
- 5.4.5 Section 16 reporting and short swing profit recapture provision.
- 5.5 Identify other possible scaling standards.
  - 5.5.1 Is size the most appropriate standard or is risk?
  - 5.5.2 Are revenues a better scaling standard for some disclosure rules and other regulations?
  - 5.5.3 Should other alternatives be considered?
- 5.6 Liability concerns.
  - 5.6.1 General.
  - 5.6.2 Safe-harbor for forward-looking information.
  - 5.6.3 Special considerations re: outside directors.
- 5.7 Consider issues of delinquent and deficient micro-cap disclosure.
  - 5.7.1 Standards.
  - 5.7.2 Cure period.
  - 5.7.3 Deregistration.
  - 5.7.4 Consider modification of Rule 15c2-11.
  - 5.7.5 Relationship with Commission delinquent filer program.
- 5.8 Evaluate the balance of disclosure to protect investors with the competitive needs of smaller public companies.
  - 5.8.1 Has disclosure gone so far that smaller public companies cannot be competitive in the global marketplace?
  - 5.8.2 What is the proper balance of disclosure?

- 5.9 Recommendations.
- 6. Accounting Principles.
  - 6.1 Evaluate “one size fits all” vs. “Big GAAP-Little GAAP.”
  - 6.2 Identify priority accounting principles, if any, where modifications might be considered for smaller public companies, including, but not limited to, stock option expensing.
  - 6.3 Emphasize importance of cash in many smaller companies.
  - 6.4 Analyze overlay and impact of other regulatory schemes (financial institutions, insurance, government contractors, etc.).
  - 6.5 Analyze role of outside audit firms with respect to smaller companies, e.g., environmental shift in role of auditors, communications with outside auditors, concentration of Big Four accounting firms, difficulty in switching audit firms.
  - 6.6 Analyze whether extended effective dates for smaller companies are appropriate for future accounting principles.
  - 6.7 Recommend changes, if any.
- 7. Capital Formation.
  - 7.1 Analyze existing structure.
    - 7.1.1 SB-1.
    - 7.1.2 SB-2.
    - 7.1.3 S-3.
    - 7.1.4 Proposed changes under '33 Act Release No. 8501.
      - \* New registration statements.
      - \* New offering procedures and rules.
  - 7.2 Analyze selected exemptions from registration and subsequent reporting.
    - 7.2.1 Section 4(6).

- 7.2.2 California Rule 1001.
- 7.2.3 Test the Waters.
- 7.2.4 Rule 701 (especially advisability of revisiting ceilings in view of increase in market standards and average time to go public).
- 7.2.5 Others.
- 7.3 Evaluate Regulation A.
- 7.4 Analyze investment banker roles.
- 7.5 Analyze analysts' coverage.
- 7.6 Costs and timing to get access to markets.
  - 7.6.1 Broader access to capital, including foreign markets.
  - 7.6.2 Possible roles of capital formation specialists, including brokers and "finders."
- 7.7. Cost of and ability to exit the markets.
- 7.7 Possible improvements in interaction and interplay between federal law or SEC, state laws or state regulators, and self-regulatory organizations and rules (e.g., Rule 15c2-11).
- 7.8 Liability issues.
- 7.9 Recommendations.
- 8. Small Business Forums and Related Issues.
  - 8.1 Analyze recommendations from recent SEC Small Business Forums.
  - 8.2 Review small business statutes (Regulatory Flexibility Act and 1980 Small Business Investment Incentive Act).
- 9. Final Recommendations.
  - 9.1 Possibility of rolling or staggered recommendations.
  - 9.2 Categories of possible solutions:
    - 9.2.1 SEC rules.

- 9.2.2 SEC staff interpretations or practices.
  - 9.2.3 PCAOB standards or staff interpretations or practices.
  - 9.2.4 SRO rules or staff interpretations or practices.
  - 9.2.5 Others (i.e., ISS, Moody's etc.).
- 9.3 Should size or other measurements be a determining factor?
- 9.3.1 If so, what should be the measurement, breakpoints, and how many levels (remember: keep it simple).
  - 9.3.2 Are there other solutions (i.e., a system based on meeting compliance and disclosure standards would relieve issuers from certain burdens; if compliance was not met, there could be additional requirements).

List of Members of the Public Who Provided Statements

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- Apr. 12, 2005 James A. Brodie, Managing Director, Carr Securities Corporation, Port  
Washington, New York
- Apr. 12, 2005 Catherine Connally, CIA, President, Issues Central Inc., Toronto, Canada
- Apr. 08, 2005 Christopher Cole, Regulatory Counsel, Independent Community Bankers of  
America
- Apr. 07, 2005 Richard D. Brounstein, Executive Vice President and Chief Financial Officer,  
Calypse Biomedical Corporation
- Apr. 07, 2005 Nelson Obus, Wynnefield Capital, Inc.
- Apr. 01, 2005 Financial Executives International
- Mar. 31, 2005 Independent Community Bankers of America