GLASS LEWIS & Co.

April 12, 2005

Mr. Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Reference: File Number 4-497
Sent via email to: rule-comments@sec.gov

Dear Mr. Katz:

The Sarbanes-Oxley Act of 2002 (SOX), including Section 404, was passed to provide investors with greater confidence in the integrity and transparency of companies and deal with abuses that arose during the internet bubble. We believe it is accomplishing its goal. While there have been those that have expressed a desire to limit its effectiveness, these calls for changes are not coming from investors who have suffered tremendous losses in recent years. Perhaps that is partially the result of approximately 2,160 companies correcting errors in their financial statements from 1997 through 2004. Indeed, while much of the debate has been around the cost companies have borne, far too little discussion has been held about the benefits that SOX has provided to investors and the capital markets.

In a 1988 release, the Securities and Exchange Commission (SEC) appropriately stated: "Complete and accurate financial reporting by public companies is of paramount importance to the disclosure system underlaying the stability and efficient operation of our capital markets. Investors need reliable financial information when making investment decisions."[1] These words echo former SEC Chairman Douglas, in an oft-quoted passage, stated:

> "The truth about the securities having been told, the matter is left to the investor. . . . The requirement that the truth of the securities be told will in and of itself prevent some fraudulent transactions which cannot stand the scrutiny of publicity."[2]

[1] Release No. 33-6789, Report of Management's Responsibilities, July 19, 1988.
[2] Protecting the Investor, William O. Douglas, 23 Yale L. Rev 521-24, 1934.

We believe the focus of the SEC should be on improving the quality of financial reporting and disclosures to investors, by ensuring investors have confidence that effective internal controls exist at companies who take money from the investing public in exchange for their stock. In that regard, we would urge the SEC to work closely with the Public Company Accounting Oversight Board (PCAOB) to study and analyze the benefits provided by SOX to investors and how the process can be enhanced and improved. We do not believe the sole focus of the discussion and study should be on the narrow topic of cost cutting measures. After all, it is clear now that cost cutting in finance functions in corporate America, as well as the auditing profession cutting back on the work it performs as a gatekeeper, has imposed tremendous costs on investors.

The Case for SOX Section 404

The accounting profession and SEC have long recognized and emphasized the importance of internal controls. Some in the business community have argued this section of SOX was hastily written and adopted, without an in-depth debate of the issue. However, this could not be further from the truth; in fact this issue has received much debate in the past within the profession, in Congress and in connection with proposals by the SEC. For example:

- In December 1977, after financial frauds and bankruptcy filings of Penn Central and Equity Funding, financial frauds at companies including Four Seasons Nursing Homes and National Student Marketing and hundreds of public companies disclosing bribes, kickbacks and political payoffs, Congress amended Section 13(b) of the Securities Exchange Act of 1934 to require issuers to have reasonable internal controls sufficient to provide reasonable assurances to investors. In 1981, an attempt was made in the U.S. Senate to delete this section of the law, but it failed.

- In 1978, *The Commission on Auditors' Responsibilities: Report, Conclusions, and Recommendations*, led by former SEC Chairman Manuel F. Cohen called for the auditors' work to be "…amplified to require a study and evaluation of controls that have a significant bearing on the prevention and detection of fraud."[3]

- On April 30, 1979, the SEC proposed rules that would have required inclusion of both a report by management and the independent auditor for the company in the annual report to the SEC and investors.

- The 1987 *Report of the National Commission on Fraudulent Financial Reporting* (the Treadway Commission) specifically recommended that the SEC require management reporting to shareholders on the effectiveness of internal control.

[3] The Commission on Auditors' Responsibilities: Report, Conclusions, and Recommendations, Page 39, AICPA, 1978.

- On July 19, 1988, the SEC once again proposed a rule that would have required including both a report by management and the company's independent auditor in the annual report to the SEC and investors.

- In 1993, the Public Accounting Oversight Board (POB) recommended in their report, *In The Public Interest*, that the SEC require management and auditor reporting on the effectiveness of internal controls.

- The 1996 General Accounting Office *Report on the Accounting Profession – Major Issues: Progress and Concerns* discussed the importance of internal controls and states: "While the accounting profession now supports internal control reporting, the SEC has not been convinced of the merits of reporting on internal control. SEC support is critical to further progress in this area. In the long run, GAO expects that audits will be expanded to include internal control reporting, either because of market demand or ***systemic crisis***." [emphasis supplied]

- *Fraudulent Financial Reporting: 1987-1997 An Analysis of U.S. Public Companies* reports that "…in 83 percent of the cases, the AAERs named either or both the CEO or CFO as being associated with the financial statement fraud." This study of financial frauds, subject of an SEC Accounting and Auditing Enforcement Release (AAER), went on to state: "The importance of the organization's control environment cannot be overstated, as emphasized in COSO's Internal Control – Integrated Framework (COSO, 1992). Monitoring the pressures faced by senior executives (e.g., pressures from compensation plans, investment community expectations, etc.) is critical."[4]

In the end, unfortunately the GAO was right. It was a systemic crisis and congressional action -- rather than a proactive SEC -- that resulted in legislation ensuring corporations have adequate controls necessary for complete and accurate financial reporting. A systemic crisis in which the New York Stock Exchange watched as the Dow Jones Industrial Average (DJIA) fell from a high of 11,723 in 2000 to a low of 7,286 in 2002. The Nasdaq experienced an even more catastrophic loss as investors watched it fall from a high of 5,048 in 2000 to a low of 1,114 in 2002. American investors began to withdraw their cash from the capital markets as trillions in value disappeared into thin air. Their faith in corporate America declined with the announcement of every additional financial fraud and as the downward spiral in the stock markets continued.[5]

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[4] Fraudulent Financial Reporting: 1987-1997 An Analysis of U.S. Public Companies, Pages 2, 4. Committee of Sponsoring Organizations of the Treadway Committee, 1999.

[5] For example, survey respondents to a CNN/Gallup Poll in July 2002 noted 73 percent of the respondents cited you "can't be too careful" with CEO's of large corporations, and only 23 percent stated you could trust them.

The drops in the stock markets were attributable to a number of factors. While a downturn in the economy was one, it was not as significant as that brought on by one financial scandal after another. While the economic recession nine years earlier had resulted in the DJIA losing 4 percent, the DJIA racked by the scandals took losses for three years in row between 2000 and 2002, losing 30 percent of its value.

As the financial frauds were exposed at companies such as Enron, WorldCom and Global Crossing, all of which had material weaknesses, the value of the stock held by investors also slumped. As noted in the attached report, we identified twenty companies from among hundreds involved in financial frauds. For those twenty companies, their stock fell over $300 billion dollars from their highs during the bubble to their lows which often resulted in bankruptcy. WorldCom was the largest bankruptcy in the history of the United States and Enron also fits within the top five.

We believe the work being done by corporations, corporate boards and independent auditors pursuant to SOX 404 will prevent the type of losses investors have suffered during this systemic crisis. Indeed, we believe SOX is accomplishing its goal of improving integrity and transparency in financial reporting by public companies. Certainly the capital markets have regained lost ground since its passage despite public opinion polls that continue to give poor rankings to corporate America. As we examine financial reports at Glass Lewis, we are seeing an improvement in transparency among many, but not yet all companies. We have also had discussions with many corporate executives and board members who have applauded the legislation for helping to restore public trust. For example, the Chief Executive Officer of a company who had gone through much of SOX in anticipation of an initial public offering noted how much it had improved the overall business. While he was certainly not ignorant of the costs, he felt they had been a worthwhile investment.

SOX has also contributed greatly to investors' confidence that financial statements and disclosures will improve in the future. During 2004 and 2005, 738 companies forewarned investors of material weaknesses in their controls. We applaud these companies for this transparent disclosure. And while hundreds have disclosed their deficiencies, as of March 31, 2005, only 227 companies have actually received reports from their auditors indicating they had a material weakness as of their fiscal year end. Based on this evidence, it is clear many companies have taken positive and corrective actions bringing their controls into compliance with Foreign Corrupt Practices Act (FCPA) passed in 1977. We also note that SOX work directly contributed to a record number of errors in financial statements being surfaced in the fourth quarter of 2004. The total number of corrections of errors in financial statements with a corresponding disclosure of material weaknesses increased 172% in 2004, growing from 67 in 2003 to 182 in 2004.

While the increased transparency and improvements in internal controls is a positive development, we must also highlight that many of the Chief Executive Officers and Chief Financial Officers of these same companies had previously certified to their investors that their internal controls were operating effectively. That certainly raises the specter that without an independent auditor testing the controls and providing their independent assessment of their findings to investors, investors would continue to be misled about the accuracy of some of the Section 302 certifications by corporate executives. This lack of transparency is certainly nothing new. For example, in 2003, 58 companies filed Form 8-K's in which they and/or their auditors reported a control deficiency, most of which had not been previously disclosed in a timely fashion to investors.

The Cost Issue

Currently, there are those who seem to be focused solely on the costs incurred by a business, with no regard whatsoever for the investment losses investors have suffered. We urge the SEC to be mindful of the two sides of costs.

We believe much of the cost issue is brought on by "deferred maintenance" or by corporations putting pressure on auditors to reduce their fees to unreasonably low levels. When auditor fees were cut "to the bone," we believe it impacted audit quality.

Indeed, cost cutting, rather than a focus on quality financial reporting is what brought us to where we are today. Certainly throughout the 1980's and 1990's, corporations, sometimes with the assistance of their audit committees, "twisted" the arms of independent auditors to reduce their audit fees. Our experience includes corporations who competitively bid their independent audit work solely to reduce their fees well below levels that could generate a reasonable return for the auditors.[6] In turn, the audit firms reduced the level of work they needed to perform in their role as gatekeepers for investors. Inevitably inferior audits resulted. For example, when analyzing fees charged by auditors for 2003 (2004 data is just becoming available) we noted 90 companies out of 461 in the Fortune 500 and 382 out of 1805 other large public companies reduced their audit fees. The auditor fees at a large national retailer declined 31% when they put their audit up for competitive bid at which time their incumbent auditor wisely declined to participate. And the audit fees at Wal-Mart were only $4.1 million dollars, substantially below the fees for any other comparable Fortune 10 size company. When it comes to audit fees, we strongly believe investors get what management pays for.

In the latter part of the 1990's, auditors also changed from testing all types of significant internal controls they were relying on each year, to cycle testing of those controls. This meant that a high technology company, where revenue recognition is a critical accounting policy and perhaps the most material amount in the financial statements, did not have its internal controls for revenue recognition tested for two years. Unfortunately, investors

[6] The Texas State Board of Public Accountancy adopted rules to address this issue.

were not informed in any manner of this cut back in audit procedures. They were misled into believing auditors were testing all significant controls on an annual basis. When material weaknesses at companies such as WorldCom and Enron were exposed, investors rightly asked "where were the auditors?"

In addition, financial reporting expertise within corporate America was also slashed. Hackett Benchmarking has reported that the cost of the finance group in corporate America was cut from 2.2 percent of revenue in 1988 to 1.15 percent at the height of the bubble. In 2000 they projected it would be further reduced to less than 1 percent.[7] At the same time, this well known consulting firm stated that activities related to fundamental accounting transactions, control and risk management are "…essential but that add no value to the business." From the view of investors in Enron, WorldCom and Global Crossing which had serious material weaknesses, we believe investors do see value in internal controls designed to ensure transactions are accounted for properly as well as identifying risks on a timely basis. Yet we note of the companies reporting material weaknesses in internal controls, 20% have stated it is due to personnel related issues.

Interestingly, as a draft of SOX was being circulated to business and accounting professionals and organizations, I remember a meeting with a large group (hundreds) of finance executives at a very large, international Fortune 20 size company. During the meeting I asked how many in the room had received any training on internal controls and the Foreign Corrupt Practices Act (FCPA) in the last ten years. The response was only one. We find it troubling that a company of this size would have such a dearth of training for its finance employees. With the implementation of SOX, no doubt much "catch up" training has had to occur.

We do believe the costs being incurred to implement SOX 404 is being driven by a lack of adequate ongoing training throughout the 1990's and into the next decade both in corporate America and the auditing firms. As a result, corporations and auditors must now incur these costs. Keep in mind SOX Section 404 did not require a single additional control, only that management ensure their controls are effective, that they report on them to the investors whose money they have taken and that auditors certify as to whether management's report is or is not correct.

We are also aware of companies that had not kept their accounting policies and procedures updated, or even worse, documented. When a company has both a lack of training and a lack of documentation instructing employees as to those key policies and procedures that are necessary for accurate financial reporting, it should not come as a surprise that there is an increase in the level of errors in financial disclosures used by investors. Based on disclosures to date, we have noted information technology security controls, critical in this digital age, have been deficient. We have noted many a company that has not gotten the basic day-to-day accounting done right. For example, in a

[7]The Book of Numbers – Finance, Page 5, Hackett Benchmarking Solutions, 2000.

conference call, one large multinational company disclosed they had to do a restatement as a result of a lack of proper and timely reconciliation of accounts over a period of time. This is consistent with one of the major financial frauds reported on the front pages of the nation's newspapers where they had not reconciled their inter-company accounts for years. In these cases, the costs to rectify and remediate these problems will be much more than the ongoing costs would have been to do the job right the first time.

Another interesting data point to consider is that we have identified a number of companies in the S&P 500 that pay their CFO's more in base pay and bonuses, than they pay their auditors. We do not begrudge these CFO's their compensation in most of these cases. However, it does raise a question as to the fairness of the fees paid to their auditors. In addition, in a number of the cases involving material weaknesses, we have noted despite these problems, the CFO's continue to receive a bonus. We find that hard to swallow for investors, when at the same time the company is complaining about the costs incurred to implement SOX.

SOX Section 404 was specifically written based on a single, integrated audit that examined the financial statements as well as the internal controls. SOX states that "Any such attestation shall not be the subject of a separate engagement." Unfortunately, as members of the accounting profession acknowledged at the November 2004 meeting of the Standards Advisory Group (SAG) of the PCAOB, the firms did not perform such audits. Instead, in many instances auditors failed to adequately design their audits to integrate the knowledge they gained from the audits of internal controls into their audits of the financial statements. This has resulted in unnecessary audit hours being incurred by independent auditors with corresponding excessive fees being charged to companies.

Small versus Large Companies

Some have argued that small companies should be given an exemption or waiver from the requirements of SOX. We strongly disagree with that view. As noted in the attached report, of the 738 companies that have reported material weaknesses in 2004 and 2005, 416 or 56% have been companies with under $200 million in market capitalization, including 168 with under $25 million in market value. We also note that companies with up to $500 million or less in revenues accounted for 65% of the approximately 842 restatements in 2003 and 2004.

We believe complete and accurate financial reporting is important for any company who chooses to become publicly listed. When a company takes money from the investing public, they agree to an obligation to provide timely and accurate financial information, regardless of their size. Accordingly, it is important, that all sizes of companies have adequate internal controls that will provide investors with reasonable assurance the financial statements have been properly prepared.

Lessons Learned – Year One

Overall the lessons learned from the first year in which management and auditors have had to report on internal controls include:

- Internal controls were deficient in many instances, some of which led to errors in financial statements being uncovered and corrected. It has also led to companies incurring significant costs as they correct these deficiencies.

- Despite requirements to certify their internal controls pursuant to Section 302 of SOX, some executives failed to disclose problems with internal controls until independent auditors became involved.

- Some companies had not performed the necessary blocking and tackling to ensure they had adequate controls, including basic functions such as reconciliations.

- Financial systems and sufficient competent personnel were lacking in many instances.

- Cycle testing of controls performed by auditors, resulting from fee pressures on auditors, left investors vulnerable to material weaknesses that have subsequently been exposed. Investors and auditors are both better off when controls are tested on an annual basis, as required by SOX.

- Audits were not well planned and integrated leading to ineffective audits costing in some instances more than they should have.

- In some instances, independent auditors created a perception that competent, independent internal auditors could not be relied on to perform procedures permitted by PCAOB Standard No. 2.

- The interactions between independent auditors, management and the audit committee have changed. Auditors are acting in an increasingly independent fashion as they should. This has resulted in financial management being required in some cases to become more responsible for their obligation and responsibility for the preparation of financial statements.

- Weaknesses in internal controls at small companies are as pervasive, or more so, than at large companies.

- Some companies, despite the SEC granting companies an additional year to get their internal controls ready, were unable to file their annual reports on time by

March 16, 2004. We noted 282 companies delayed their filings, of which 137 were due to issues related to internal controls. This raises further concerns about the adequacy of internal controls at these companies as they had over two and a half years after the passage of SOX, and over 27 years after the passage of the FCPA. It appears as if many of these companies simply procrastinated until the last minute when it became to late to fulfill their obligations to their investors.

Impact on Relationship Between Management and the Independent Auditor

The obligation for preparing accurate and reliable financial statements rests with management of a company, not the auditors. It is the role of the independent auditors, once management has prepared the financial statements, to examine them and either concur or disagree with management as to whether they fairly present the financial condition and results of operations in accordance with generally accepted accounting principles.

A concern we have as users of financial statements, is the number of times we have spoken with a CFO or even a controller, who have expressed that they do not have sufficient expertise to properly prepare the financial statements and fulfill the basic requirements of the Securities laws. For example, one such discussion involved a Fortune 500 company whose lease accounting was questioned by its auditor and ultimately the SEC, resulting in a significant restatement. Yet in our discussions with representatives of the company, we learned its CFO and controller did not have the ability to interpret and apply the lease accounting rules. In another case involving a mid cap size company, a discussion with the CFO and controller identified they too did not have an understanding of GAAP related to an issue their auditor was requiring a restatement for. In that case, there was “black and white” accounting guidance directly on point, and it took us less than 15 minutes to determine the auditor was correct. This past year, in a Midwestern based company, we watched as the auditors correctly demanded a change in management when existing management proved their incompetence in dealing with the auditors in a very inept fashion, contributing directly to a decline in the price of the stock at the time. Accordingly, it is not surprising that 20% of the material weaknesses cited by companies to date, involve personnel issues.

We have heard all too frequently a CFO or controller blame their auditors for errors in the financial statements the CFO and/or controller had prepared. I recall a meeting with 40 to 60 such individuals in public companies who stated it was the auditor’s fault if numbers were not correct, but not their fault. I have also recently seen a litigated case in which the company’s defense was it was the auditor who told them what the accounting should be, and therefore it was the auditor, not management or the company that should have to pay any claims. It should not come as a surprise to management that if they act so irresponsible, independent auditors will react in what we believe is an appropriate fashion.

Based on our combined experiences as CFO's, controllers and financial personnel, as well as auditors and corporate board members, we believe it is entirely appropriate that auditors are once again acting as an independent examiner of the work performed by management. We believe auditors are correctly once again requiring management to prepare the financial statements, analyze and determine the proper accounting for transactions. When it is the auditor who has determined the proper accounting, it is impossible for that profession to then audit their own work and conclude in an objective fashion as to whether it is correct. Accordingly, we applaud the efforts of auditors who taken appropriate steps to once again become the independent party Congress initially intended them to be.

The person who hires, evaluates and fires the auditor has also changed from management to the audit committee comprised of independent board members. Whereas in years gone by, auditors earned a large portion of their revenues from consulting contracts awarded by management, today's auditing firm is much more dependent on the revenues produced by performing high quality, independent audits. As a result, we believe auditors who have been more concerned in the past with how to please management to generate consulting revenues, now are more concerned with the quality of their audits of financial statements and accompanying disclosures. This cannot help but influence behavior in the board room, and we think it is a positive development.

Recommendations for Continuous Improvement

We believe the SEC and PCAOB should undertake to assess the benefits companies have incurred as they have improved their internal controls. An assessment of benefits investors have received is also necessary to make an informed analysis of all costs and benefits associated with implementing SOX Section 404.

We believe that at this time, revisions to SOX Section 404 and PCAOB Standard No. 2 are unwarranted and not necessary. We do believe implementation guidance should be provided and may be done within the context of the existing rules.

We believe that costs incurred by companies will be reduced in 2005 and hopefully further reduced in 2006. This will be due to a reduction in costs paid to outside consultants hired to assess and implement their internal controls, documentation of internal controls having occurred and been brought up to date in 2004, and personnel at companies having gone through a steep learning curve. In addition, auditors have publicly stated their intent to redesign their audits to become integrated audits. Auditors should also be better trained, in part as a result of the extent of "on the job training" that occurred in 2004. This training of the auditors no doubt also consumed countless hours of company personnel.

We are concerned with respect to the level of detail many respondents to the SEC roundtable have requested in additional guidance. It certainly is not founded in a principle based approached, and we fear that if many of the recommendations are adopted, existing standards will expand beyond the shelf space required for the tax code. More important than new guidance, we believe financial management and auditors need to apply a little common sense and reasonable judgment. We have found the regulators are sufficiently flexible with public companies when sound judgment is applied, as opposed to the unreasonable level of judgments used by preparers and auditors in some of the companies listed in the attached report that engaged in financial fraud.

We believe the PCAOB should use the knowledge gained from their inspections in preparing implementation guidance. They could and should do limited inspections of work performed by auditors in preparing that guidance. That means the Board may well have to advance some of its inspection work which it should do. However, we urge the SEC and PCAOB to be diligent and thoughtful in this exercise and not try to rush out guidance in response to political pressures before it is ready. For example, imposition of artificial deadlines does not result in quality guidance.

We believe the PCAOB should:

- Prepare a question and answer document responsive to the most common questions audit committee members have. This would require interaction with a group of audit committee members which we believe would be beneficial for both sides.

- Clarify that independent auditors can rely on internal auditors who are independent and qualified.

- Issue an interpretation that we believe would be consistent with PCAOB Standard No. 2 that states that after the initial year of implementing and testing controls, management can rely on effective monitoring controls as a basis for its assessment, provided management or the internal auditors have tested those controls, on a test basis, and found them to be effective. We believe within the guidelines of Standard No. 2, management should be able to rely on monitoring controls combined with internal auditors performing tests of both monitoring and basic internal controls. In turn, we believe auditors should have to perform sufficient tests of internal controls, especially those related to fraud prevention, material account balances and high risk subjective judgments. However, independent auditors should be able to rely on testing of controls over the processing of basic day-to-day transactions, less risky and less material accounts. We continue to agree with Standard No. 2 that the independent auditor should have to perform an annual walk through for controls over fraud prevention, material and high risk accounts and subjective judgments.

- We believe the PCAOB should use their inspection process to encourage independent auditors to apply Standard No. 2 and SOX Section 404 as they were intended. This is especially true for audits of smaller companies.

- We believe the one size does not fit all approach in Standard No. 2 should be emphasized by the PCAOB. We believe, for example, smaller companies should be encouraged to explore efficient methods of documenting their internal controls such as through flow charts or questionnaires that could also be used by the independent auditors. We believe the PCAOB should examine the approach auditors are using, including checklists that may be employed, to ascertain whether they meet the "common sense" test, including for smaller companies.

- Create a roundtable of CFO's, auditors, investors and regulators to develop best practices in how companies and their auditors should address and resolve accounting and communication issues. Such best practices should be published in a document similar to that developed for auditors in the mid 1990's for how they would consult with the SEC.

We oppose the efforts of some who believe the independent auditors may perform less than a majority of the testing and yet still issue an independent audit report on internal controls. For example, some believe internal auditors may perform a majority of the testing but have the audit report to investors be signed by the independent auditor. We believe this is misleading to investors and lacks transparency. We believe it will lead to an increase in the current "expectation gap" that exists between investors and auditors. If such an approach is adopted, we believe the auditors' report should clearly state the extent of the work they have performed and the extent of work others have performed that the auditor is relying on.

We believe there should continue to be an annual assessment of internal controls. Cycle testing of controls is what occurred in audits leading up to investors suffering tremendous losses in many companies, and a return to that approach should not adopted. It provides insufficient transparency and protection for investors and is a significant rollback in the implementing rules. It is also inconsistent with the language of SOX which requires management make an assessment at the end of each fiscal year of its internal control structure and that the auditor report on that assessment. The notion of cycle testing, which failed investors so miserably during the stock market bubble, is never mentioned in SOX. If cycle testing were once again implemented, we believe it would be important for the auditor's report to clearly state what controls have been tested and those that have not, and for how many years they have not been tested. We believe any less transparency is an intentional deception of investors.

We concur with the statement of the Financial Executives International that auditing firms should have to adopt some of the same requirements imposed on public companies for the purpose of transparency. In this regard we believe auditing firms should have to make all of their inspection reports and audited financial statements public. We also believe they should be required to have independent boards of directors, similar to public companies.

Conclusion

We believe that SOX has resulted in significant benefits to investors, the capital markets and public companies. A focus on continuing to enhance and improve these rules is commendable. However, a focus simply on cost cutting will only bring us full circle and result in history being repeated.

We appreciate the opportunity to present at the SEC Roundtable. We would be pleased to further discuss this letter with the SEC staff at its convenience.

Cordially,

Lynn E. Turner

Lynn E. Turner
Managing Director
Glass, Lewis & Co., LLC

Attachment

cc: Mr. William J. McDonough, Chairman PCAOB
Mr. Douglas R. Carmichael, Chief Auditor, PCAOB
Mr. Donald T. Nicolaisen, Chief Accountant, SEC

April 12, 2005

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YELLOW CARD
INTERIM TREND ALERT

Internal Control Deficiency Disclosures – Interim Alert

Summary

In our view, strong, effective controls are an integral part of quality financial reporting. Effective internal controls are good for both investors and a well-managed business, in our view. We believe the effects of the internal control aspects of the Sarbanes-Oxley Act should be allowed to run their course, as preliminary results as of March 31, 2005 show no definitive trends. Our findings show the following:

- Control assessments and audits have already contributed to the discovery and correction of material errors at numerous companies.
- The CEOs and CFOs of the majority of companies disclosing a material weakness in 2005 had previously certified their company's controls as effective under Section 302 requirements. Consequently, we believe only an audit has "held their feet to the fire" and prompted them to actually perform a thorough assessment of internal controls.
- For companies who complain that the cost of implementation is too burdensome, we question why CFO compensation does not appear to have been lessoned for companies who find problems. If cost reductions are necessary, we feel bonuses for executives who fail in their obligations to investors should be on the chopping block.
- We do not see a significant predictive trend in stock price changes for companies disclosing material weaknesses or significant deficiencies.

Much data remains to be analyzed as many companies have just filed their reports on internal controls and many more still have to do so. Until that data is received and analyzed, we believe it would be premature to revise the Sarbanes-Oxley Act. However, enhanced disclosure requirements would allow investors to gain a better understanding of how a material weakness or significant deficiency may affect future financial results.

Effective controls contribute to more accurate and reliable financial information

We strongly believe effective internal controls contribute to more accurate and reliable financial information, especially for information that is not subject to audit such as press releases and quarterly financial statements. More reliable information aids both internal and external decision makers in operational and investment decisions.

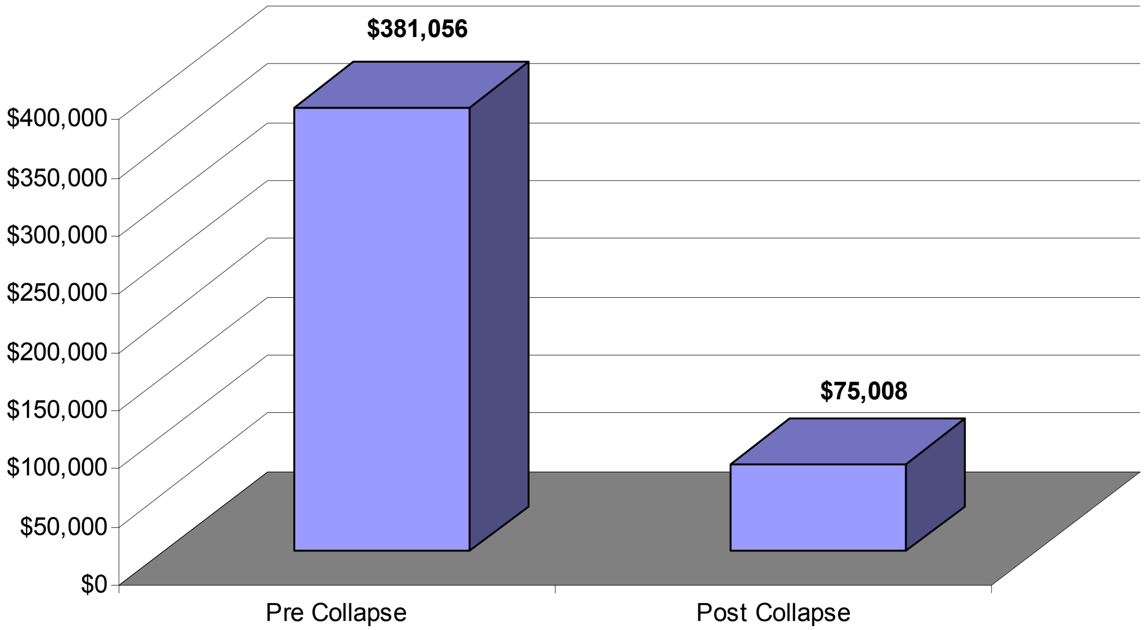
In our view, having strong, effective controls may also aid investors by providing a deterrent against intentional fraud. While admittedly difficult to measure the benefit, we feel the fear of getting caught may discourage frauds and defalcations. Also, the increased scrutiny by auditors, the Public Company Accounting Oversight Board (PCAOB), and the Securities and Exchange Commission (SEC) may create more awareness of the issues that initiated frauds in the first place, thus stopping them before they even start, in our opinion.

Cost versus benefit debate

The cacophony of complaining in the business community over the significant costs related to complying with the internal control requirements seems to be louder than the cheers for its benefits to investors, in our view. According to a study by Financial Executives International (FEI), the cost to implement the internal control requirements of Sarbanes-Oxley averaged $4.4M per company. If that number were extrapolated to the entire market, total costs of implementation for approximately 5,500 accelerated filers would be $24B. However, we feel that loss prevention, though difficult to measure, outweighs any increased administrative costs. In our opinion, the cries of hardship are probably coming from the companies with the worst controls. Naturally, we would expect these companies to have the largest burden to implement necessary but nonexistent controls or remediate ineffective controls before any testing can even begin.

The enormous investor losses from the past few years are quickly forgotten even though investors continue to pay in other ways. Chart 1 shows the market capitalizations of 20 well-publicized accounting collapses as they fell from their high during the bubble to their lows as their false and misleading financial results became transparent to investors (see appendix for details of each company). The difference between the high and the low represents a $306B decline in shareholder value.

Chart 1: Shareholder Losses ($ in millions) from 1997-2002 Accounting Scandals



Source: FactSet, GLC. Companies include Global Crossing, Krispy Kreme, Critical Path, Network Associates, Rite Aid, Lernout & Hauspie, Symbol Technologies, HealthSouth, Oxford Health Plans, Adelphia, MicroStrategy, Waste Management, Cendant, Qwest, WorldCom, Enron, Tyco, Peregrine Systems, McKesson HBOC (MCK), and Sunbeam. See appendix for further details.

In addition to the losses shown in Chart 1, investors are still paying the price indirectly for inaccurate financial information. For example, Citigroup and JP Morgan recently settled with WorldCom shareholders for $2.75B and $2B, respectively. According to a study by National Economic Research Associates (NERA), even though actual monetary settlements have increased, as a percentage of shareholder losses, litigation settlements have decreased. In our view, this may have been caused by the sheer enormity of some of the shareholder losses. We believe these trends highlight why effective internal controls necessary for integrity and quality of financial reporting have been required by law since 1977.

Errors leading to restatements found during control reviews

For those more skeptical of the monetary benefits of strong internal controls, we recommend reading a few of the Form 8-K Item 4.02 disclosures which provide details on why companies are restating their financial statements. For example, **Meadwestvaco** (MWV), **International Paper** (IP), and **Bancinsurance Corp** (BCIS) all disclosed that their internal control reviews led to the discovery of material errors in prior financial statements related to deferred tax liabilities, reinsurance claim reserves, and foreign currency translation adjustments, respectively. Although we cannot say with certainty that the errors would or would not have been found by some other audit procedure later, each Company attributed the error discovery to internal control reviews. Other companies, such as **Sapient Corporation**

(SAPE), have disclosed the need for material audit adjustments due to errors in 2004 financial statements that were detected through internal control reviews.
We believe there is a direct relationship between control deficiencies and financial statement errors. Before Sarbanes-Oxley, disclosures of internal control deficiencies were only found in a Form 8-K for the announcement of an auditor change. Our analysis of 2003 auditor turnover showed that 58 companies (all with market capitalizations over $100M) disclosed having some sort of control deficiency in 2003. Of this 58, eight companies again disclosed deficiencies or weaknesses in 2004 - an indication that the companies did not take the appropriate actions to correct the problems.[1] A restatement was later announced at three of these companies – **Audiovoxx (VOXX), Collins & Aikman (CKC), and Inverness Medical (IMA)**. In our view, the progression of uncorrected material weaknesses is a potential restatement.

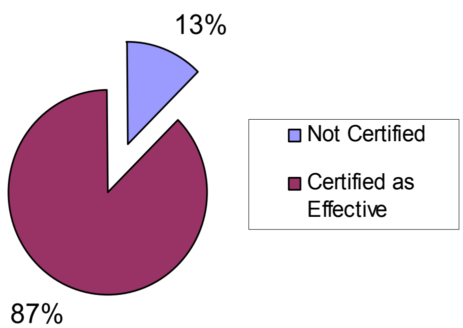
Management's ignorance of control deficiencies is not bliss for investors

We feel the recent conviction of Bernie Ebbers of WorldCom infamy illustrates perfectly that ignorance claims do not relieve culpability. As for internal controls, 87% of the 2005 companies noted in our study claimed that their controls were effective as recently as the Form 10-Q prior to their revelation of a control deficiency (Chart 2).

If a tree falls in the forest and no one is around, does it still make a sound?

In our view, the control deficiency probably did not appear overnight. Consequently, we feel that the problem most likely existed in prior quarters, and management failed to properly identify the problem and disclose it in a meaningful, transparent manner to investors, especially at companies who have announced a restatement spanning several years.

Chart 2: Percentage of 2005 Companies who Announced Control Issues Despite Previously Certifying Controls



Source: FactSet, Company Reports, GLC. 2005 includes disclosures through March 31, 2005.

Many companies disclosed some control problems were only found after an external auditor began their procedures. We feel this may be a signal that companies may not have put forth a good faith effort in assessing their internal controls despite the certification requirements that have been in place since 2002. In our opinion, the honesty of disclosures made to investors is called into question if management simply "rubber-stamps" Section 302 certifications without thoroughly investigating the accuracy of their statements. This is especially true when an external audit reveals issues not previously disclosed by the CEO and CFO. It appears to us the requirements of Section 404 played a significant role in changing the assessment of internal controls from an "eyeballed estimate" to a more thorough audit.

According to Compliance Week, 582 companies warned investors of potential control problems in 2004, 314 of which warned of a material weakness. An additional 424 have warned of material weaknesses in 2005. Of these who have

[1] Audiovoxx (VOXX), Cellstar (CLST), Collins & Aikman (CKC), Danka Business Systems (DANKY), DHB Industries (DHB), DVI Inc. (DVI), Inverness Medical (IMA), and Tarrant Apparel Group (TAGS).

since filed an annual report, we have noted only 46 who have received an unqualified opinion.[2] In the meantime, some of the companies have corrected their deficiencies.

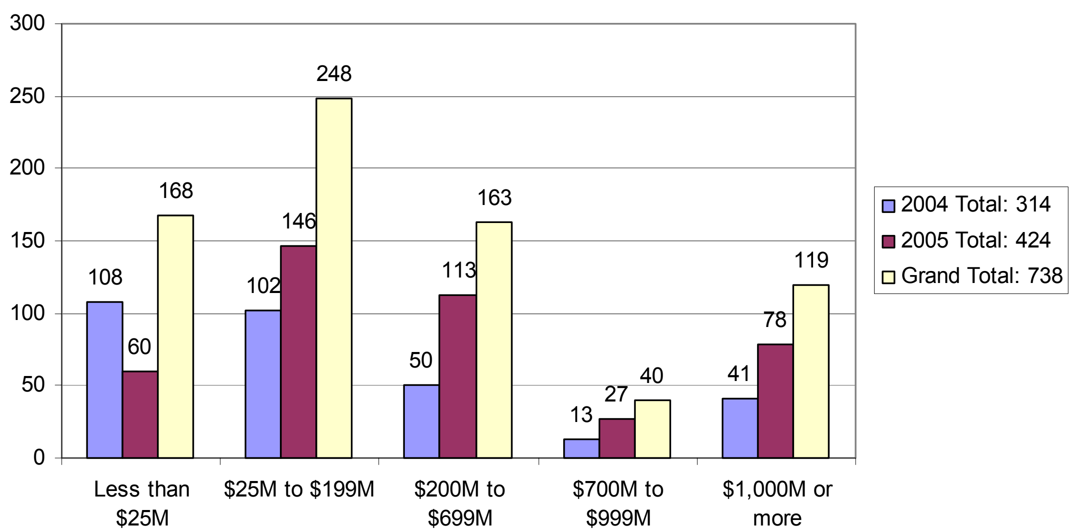
However, we have noted 171 companies did not warn investors in an SEC filing that an adverse opinion was imminent, yet an adverse opinion was included in their annual report filed by March 31, 2005. If 2004 and the first quarter of 2005 are setting a precedent, we may see a significant number of companies report a material weakness when their internal control opinion is issued even though they are currently certifying their controls as effective.

Companies disclosing control deficiencies

Different compliance timelines and extensions have made determining the percentage of filers disclosing a material weakness or significant deficiency difficult. Generally, large accelerated filers (markets capitalizations over $700M) were required to have an audit of their internal controls for annual periods ending after November 15, 2004. Consequently, most large calendar year end companies had to comply with the rules starting with their annual report for the year ended December 31, 2004. The SEC granted a 45-day extension for smaller accelerated filers (market capitalizations under $700M). The extended deadline would be April 30, 2005 for any company wishing to utilize the extension. Non-accelerated filers (generally those companies with market capitalizations under $75M or who have never filed an annual report) have an additional year before an audit of their internal controls and report thereon is due. Therefore, our preliminary analysis of disclosed control deficiencies (including material weaknesses, significant deficiencies, and reportable conditions) may not be indicative of the future results of other companies.

The existence of control deficiencies is not merely a problem faced by large companies. Chart 3 includes all disclosures of material weaknesses we have noted in 2004 and 2005 through March 31, 2005. This includes those companies who warned investors of issues prior to their filing an annual report as well as those who did not warn investors but have received a qualified audit opinion on their internal controls.

Chart 3: 2004 and 2005* Material Weakness Disclosers by Market Capitalization



Source: FactSet, Company Reports, GLC. *2005 includes disclosures through March 31, 2005.

[2] We have tracked 314 companies in 2004 and 424 companies in 2005 that have disclosed material control weaknesses. Other companies have disclosed the existence of potential significant deficiencies or reportable conditions that do not constitute a material weakness. Compliance Week has published 582 companies that reported a material weakness, significant deficiency, or reportable condition in 2004.

Chart 3 shows that small companies disclosing a control issue have outnumbered large companies. We find this interesting since small companies (many may be non-accelerated filers) have an extra year before they are required to comply with the internal control audit requirements of the Sarbanes-Oxley Act and the smaller accelerated filers were given an extension. On the other hand, we feel it may also indicate companies' recognition that they should disclose a negative finding when it is discovered as opposed to waiting until the internal control audit opinion due date.
The increase in announcements year over year, even though our data included only those announcements as of March 31, 2005, shows that the trickle of disclosures that began in 2004 became a flood of revelations as the March 16, 2005 filing deadline drew near.

Types of control deficiencies disclosed

Since we believe the severity of a control weakness depends on how the issue will affect the financial statements, we have assigned each weakness to one of five categories (Table 1). Table 1 includes only companies reporting a material weakness and as such does not include those disclosing significant or lesser control deficiencies. Our categories include:

1) Financial systems and procedures – general ledger systems, accounting software, or review or cut-off procedures
2) Personnel issues – lack of competent finance/accounting staff or insufficient staffing levels
3) Documentation – failure to retain adequate supporting information for accounting transactions
4) Revenue recognition – failure to apply the correct accounting guidance to revenue
5) Other

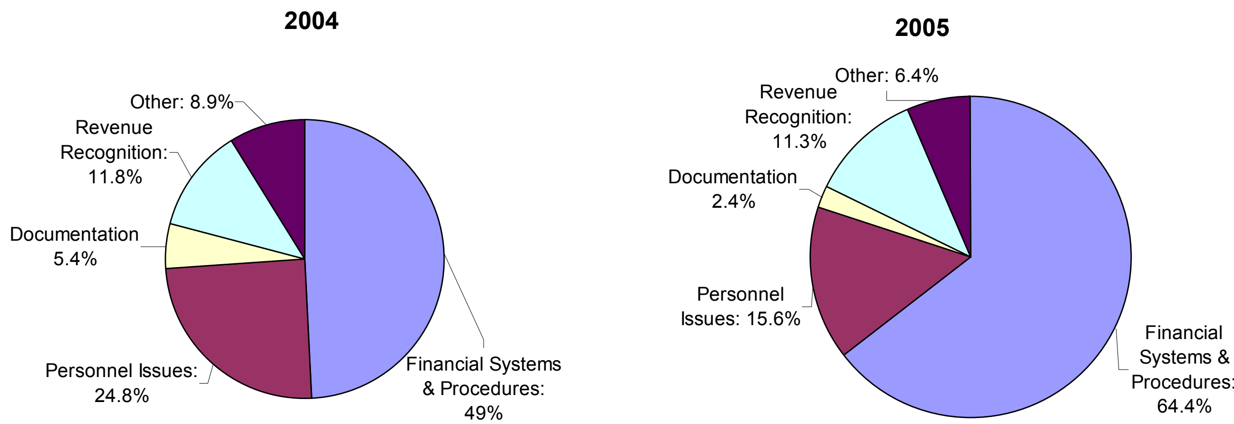
Table 1: 2004 and 2005 Material Control Weakness Classifications

Material Weakness Classification	2004	2005	Total
Financial Systems & Procedures	154	273	427
Personnel Issues	78	66	144
Documentation	17	10	27
Revenue Recognition	37	48	85
Other	28	27	55
Total	314	424	738

Source: Company Reports, GLC. Note: 2005 data is through March 31, 2005.

Chart 4 shows our classification categories as a percentage of the total material weaknesses disclosed during and 2004 and through March 31, 2005.

Chart 4: Classified Percentage of Material Control Weakness and Significant Deficiencies by Year



Source: FactSet, Company Reports, GLC. Note: 2005 data is through March 31, 2005.

Of the 738 companies who disclosed a material weakness in 2004 and 2005 (through March 31, 2005), only 262 have filed an annual report which includes an audit opinion on internal controls. Table 2 shows that of the companies previously disclosing a material weakness in 2004 and the first three months of 2005, 204 companies have received an adverse opinion on their internal controls. Most of these companies have not yet filed their report on effectiveness of internal controls due to the use of the 45-day extension, or their annual report is not yet due because of their year-end or non-accelerated filer status.

Table 2: Outcome of Opinions on Material Weaknesses

Descriptions	#
Adverse opinions	204
Non-timely filers that expect an adverse opinion	6
Disclaimed opinions	6
Total negative opinions	216
Unqualifed opinions depsite prior warning	46
Reports not yet filed:	
Using 45 day extension	40
Non calendar year-end	167
Non-accelerated filer	122
Other*	147
Total material weakness announcements	738

Source: FactSet, Company Reports, GLC. Adverse opinions are as of 3/31/05.
*Companies have included only limited information about the status of potential weakness or when a control opinion will be received.

Table 3 shows the number of adverse opinions by auditor issued in 2005 through March 31, 2005 for these companies. As a percentage of total public companies audited who are required to file reports with the SEC, no audit firms stands out as issuing a more significant number of adverse internal control opinions. According to Corporate Executive Board, approximately 70% of accelerated filers had filed their annual reports with the SEC as of March 31, 2005.

Table 3: Adverse Opinion by Audit Firm

Audit Firm	Total	Adverse as % of Total	Public Cos Audited*	% Public Cos Audited
Deloitte & Touche	31	15%	1,296	2%
Ernst & Young	49	24%	2,856	2%
KPMG	40	20%	1,893	2%
PwC	57	28%	3,234	2%
BDO Seidman	7	3%	283	2%
Grant Thornton	13	6%	424	3%
Other	7	3%		
Total	204	100%		

Source: FactSet, Company Reports, *Public Accounting Report, GLC. Adverse opinions are as of 3/31/05.

CFO compensation unaffected by internal controls

For all the cries of suffering caused by the supposedly exorbitant internal control implementation costs, the pocket books of the CFOs of companies disclosing some type of control deficiency do not seem to be suffering. Our evaluation included a review of executive compensation for those companies who had disclosed a material weakness in internal controls. Specifically, we were looking for those companies which increased CFO bonuses or stock compensation despite the fact the company had serious fundamental control problems. These problems were evidenced by a disclosure of a 2004 material weakness in internal controls as well as a recent restatement in the company's financial statements. For companies that restated in 2004, only six out of 34 failed to receive a bonus. For those receiving a bonus, as a percentage of salary, the bonus ranged from a low of 11% to a high of 182% and an average of 70%.

Our analysis uncovered several companies which we considered the compensation egregious in light of the accounting problems. In our view, three of the more blatant examples are shown in Table 4.

Table 4: Increasing CFO Compensation Despite Material Weaknesses & Restatements

				2004 Compensation			2003 Compensation		
Company Name	Name	Title	Date Became CFO	Salary	Bonus	Stock	Salary	Bonus	Stock
El Paso Corp. (EP)	D. Dwight Scott	CFO	10/2002	$453,929	$498,644	$739,200	$517,504	$750,000	$0
Goodyear (GT)	Richard J. Kramer	CFO	6/1/2004*	$378,750	$587,704	$0	$0	$0	$0
SunTrust Banks (STI)	John W. Spiegel	CFO	08/2000	$455,000	$504,140	$0	$500,000	$400,000	$239,918

Source: Company Reports, GLC. *Prior to being named CFO, Mr. Kramer had served as Goodyear's principal accounting officer until August 2002.

Gas transportation and storage company El Paso Corporation has experienced a litany of accounting problems over the past several years. In fact, El Paso has been required to restate its financial statements three times in the last two years due to errors ranging from inaccurate reserve estimation techniques to improper acquisition accounting to improper accounting for a discontinued subsidiary. The annual periods affected by these restatements range from 1999 to 2003. In addition to the restatement issues, El Paso has disclosed material weaknesses in each of its last two annual reports. Most notably, the weaknesses related to a lack of security over access to computer systems used by both IT and the financial reporting and accounting staff. Other control problems included poor account reconciliation procedures within the accounting department as well as a general inability to properly interpret and implement complex accounting standards. Despite what we view as an abysmal track record with its internal accounting and overall system of internal accounting controls and despite the fact the internal control problems still haven't all been fixed, the El Paso CFO was paid in 2004 a $0.5M bonus and nearly $0.75M in stock compensation.

Goodyear has also disclosed material weaknesses in each of its last two annual reports. In addition, Goodyear has restated its financial statements twice in the last two years. The first restatement was a result of a review of internal controls which found issues relating to un-reconciled accounts. The second restatement was required after management uncovered widespread fraudulent accounting in its European Union Tire business segment as well as accounting irregularities resulting in the understatement of the company's workers' compensation liability. The annual periods affected by these restatements were 1998 through 2002. Goodyear's current CFO, Richard Kramer joined Goodyear in March 2000. One month later, Mr. Kramer was elected Vice President-Corporate Finance, serving in that capacity as the Company's **principal accounting officer** until August 2002[3]. Mr. Kramer became Goodyear's CFO in June 2004. Despite the fact that Mr. Kramer was Goodyear's principal accounting officer for a large part of the periods which were restated and despite the fact the internal control problems still haven't all been fixed, Goodyear management paid the CFO nearly $0.6M in 2004 bonuses.

In October 2004, SunTrust Banks announced it was restating the financial statements for the first two quarters of 2004 due to a misstatement in the Company's allowance for loan losses. A similar restatement had been required in 1998. The misstatement was a result of errors and internal control deficiencies. In January 2005, the Company officially disclosed a material weakness in internal controls relating to the process for establishing the allowance for loan and lease losses. Despite the required restatement as well as the corresponding identification of a material weakness over one of the most critical accounts in a bank's balance sheet, SunTrust's CFO received a 25% increase in his 2004 bonus.

Mixed reaction from marketplace

Our analysis of the stock price changes during various time periods surrounding the 2004 announcements of a control deficiency (includes material weaknesses, significant deficiencies, and reportable conditions) showed no conclusive trend in stock price change related to the disclosure.[4] Although the arithmetic mean may have predicted a decrease is stock price based on certain data stratifications, the large standard deviations indicate that the stock price's change varied significantly. We feel it is appropriate to individually evaluate the severity of any control deficiency disclosure in relation to other factors that may be affecting a particular company.

In Tables 5 and 6, we show the ten companies (all with market capitalizations over $100M that disclosed a material weakness in 2004) experiencing the most significant percentage changes in stock price from one day prior to 30 days after the announcement of the material weakness in internal controls.

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[3] Obtained from Reuters' Company Officers' Biographies - http://yahoo.investor.reuters.com.

[4] Analysis of the 2005 announcements is still preliminary due to the timing of this report.

Table 5: 2004 Largest Decrease in Stock Price for Companies with a Material Weakness (over $100M Market Cap)

Ticker	Company	Day Before	30 Days After	% Change	Remediation?
SOL	Sola International Inc.	19.95	15.95	-20%	N
GT	Goodyear Tire & Rubber	9.92	7.90	-20%	N
ASYT	Asyst Technologies	5.20	4.13	-21%	N
FRED	Fred's Inc.	18.32	14.48	-21%	N
SANM	Sanmina-SCI Corp.	8.11	6.37	-21%	N
LU	Lucent Technologies	4.42	3.38	-24%	N
SYXI	Ixys Corp.	9.00	6.62	-26%	N
PRSFE	Portal Software Inc.	4.50	3.09	-31%	N
STEM	StemCells	4.09	2.66	-35%	Y
GLBC	Global Crossing	19.85	8.80	-56%	N

Source: FactSet, Company Reports, GLC.

Table 6: 2004 Largest Increase in Stock Price for Companies with a Material Weakness

Ticker	Company	Day Before	30 Days After	% Change	Remediation?
WJCI	WJ Communications	2.21	3.69	67%	Y
CNR	CanArgo Energy Corp.	0.73	1.21	66%	Y
DHB	DHB Industries Inc.	6.05	8.60	42%	N
WGAT	WorldGate Communications	1.90	2.70	42%	Y
ARS	Commonwealth Industries	10.62	14.89	40%	N
VXGN	Vaxgen	11.24	15.38	37%	N
IES	Integrated Electrical Services	3.93	5.22	33%	N
CKCM	Click Commerce	9.96	13.13	32%	N
MTZ	MasTec	4.46	5.83	31%	N
ENER	Energy Conversion Devices	13.26	16.84	27%	N

Source: FactSet, Company Reports, GLC.

We find it interesting that few of the companies in either group mentioned having a remediation plan in place when first disclosing the material weaknesses.

Recommendations

Based on our reviews of hundreds of public filings, we recommend the SEC and companies enhance disclosures about control deficiencies. For example, we noted many companies who simply stated they had material weaknesses related to financial systems and procedures without adding more detail (literally). From an investor's viewpoint, we find such a disclosure difficult to evaluate. By definition, a material weakness means that the control could lead to a potentially material error in the financial statements. However, more information about what potential errors may occur would be useful. Would the error be related to an understatement of accounts payable or to the accounting for derivatives? Without more information, we believe an investor is left without a way to evaluate the severity and magnitude of a potential error.

In our opinion, each control deficiency must be evaluated in the context of a company's operations and the weakness's impact on future results. The type of material weakness should be evaluated based on whether or not it changes an investor's view of the quality of earnings or cash flows. For example, revenue recognition issues that impact the historical trend and forward projections may be more severe than a control deficiency that is isolated to one operating location or balance sheet.

Also, remediation efforts to correct the material weakness are important items to be included in disclosures. Swift remediation may indicate that management at least values quality and accurate reporting. In our opinion, no such disclosures signal to investors that the issue may be costly to fix, may take a long time to correct, or management is not taking seriously its duty to provide accurate, reliable information to investors. We feel that more questions left unanswered in the disclosure translate into being less comfortable that management has provided all relevant information and assurance that the deficiency is not a continuing problem that will impact forward projections.

Additionally, more information may come to light as the remaining 30% of accelerated filers file their annual reports throughout the course of 2005.[5] Making changes based on preliminary, inconclusive results may not be in the best interest of any parties involved, in our opinion. Accordingly, we believe it is too early to make any changes to the existing rules and encourage investors and regulators to stay the course.

[5] FactSet data shows that there are roughly 5,500 companies with market capitalizations over $75M.

Appendix:

Market capitalization losses

Stock prices can be substantially impacted when the integrity and credibility of financial information is in doubt. When investors learn that amounts reported in financial statements are incorrect, they may revise their assessment on the perceived value of the firm in question. Two separate analyses have been performed (Tables A1 and A2), which assesses the market impact of restatements. The first table looks at the immediate, short-term impact, while the second table evaluates the longer-term effects.

Shareholder losses based on date accounting issue announced

The first analysis reviews the impact on stock prices when a Company, or another external source, announces that accounting problems exist at the Company. Table A1 measures the decline in market capitalization during the period beginning two days prior to the announcement of the intention to restate (or in the absence of such an announcement) the filing date, and the ending five days following that date. The analysis concludes that when an announcement is made that calls into question the reliability of financial reporting, the loss to investors can be substantial. Of the 20 companies reviewed in this study, the market capitalization lost between the two days prior to the reporting of a restatement and the five days following that date was $175B, or (51)%.

Table A1: Market Cap Declines from Two Days Before to Five Days After Disclosure of Accounting Events

Company Name	Ticker	Announcement Date	7 day Mkt Cap Loss ($ in millions)	Cumulative Return
Global Crossing (1)	GX	7/27/01	(281.8)	-4.2%
Krispy Kreme (2)	KKD	5/7/04	(735.1)	-37.0%
Critical Path (3)	CPTH	2/6/01	(9.3)	-7.1%
Network Associates (4)	MFE	12/26/00	(800.0)	-55.0%
Rite Aid (5)	RAD	10/11/99	(744.4)	-23.0%
Lernout & Hauspie (6)	LHSP	9/21/00	(1,090.6)	-47.0%
Symbol Technologies (7)	SBL	2/13/02	(1,569.5)	-48.7%
Health South (8)	HLSH	8/27/02	(2,638.3)	-55.6%
Oxford Health Plans (9)	OHP	10/27/97	(3,558.5)	-65.3%
Adelphia (10)	ADELQ	3/27/02	(1,549.7)	-47.8%
MicroStrategy (11)	MSTR	3/20/00	(19,551.2)	-61.3%
Waste Management (12)	WMI	7/7/99	(11,842.2)	-34.7%
Cendant (13)	CD	4/15/98	(13,000.1)	-42.1%
Qwest (14)	Q	7/27/01	(5,654.2)	-12.4%
WorldCom (15)	WCOM	6/26/02	(6,962.7)	-100.0%
Enron (16)	ENE	10/12/01	(11,519.0)	-43.8%
Tyco (17)	TYC	1/14/02	(77,478.7)	-74.1%
Peregrine Systems (18)	PRGN	5/6/02	(192.6)	-38.1%
McKesson HBOC (19)	MCK	4/22/99	(8,031.7)	-45.6%
Sunbeam (20)	SOC	4/3/98	(1,468.3)	-33.1%
	TOTAL		(168,677.8)	-50.3%

Source: GLC, Capital IQ, BigCharts.com. Note: Companies in the above table were selected based on the large market capitalization changes associated with their accounting announcements. The data is not adjusted for other market changes occurring during the respective time periods affecting each firm.
(1) July 27, 2001, the former VP of Finance sent a letter to the Company alleging fraud.
(2) May 7, 2004, the Company announced first quarter earnings shortfall.
(3) February 6, 2001 the Company announced that the Board was investigating the revenue recognition practices.

(4) December 26, 2000, the Company announced at its earnings press release senior management changes and that it would change its revenue recognition policy.
(5) March 12, 1999, the Company announced an earnings shortfall for the 4th qtr.
(6) September 21, 2000, the Wall Street Journal reports that an SEC probe of L&H's financial statements is in the works.
(7) February 13, 2002, Newsday, Inc. issued an article about accounting problems at the Company.
(8) August 27, 2002, the Company announced an earnings shortfall for fiscal year 2002 and that it was replacing the CEO.
(9) October 27, 1997 the Company announced in a press release that they would take a charge of between \$47 to \$53 million in the third quarter due to accounting irregularities.
(10) March 27, 2002, during the conference call for the 2001 results, an analyst asks the CFO about off-balance sheet loans made to the Rigas family, but the CFO is unable to answer.
(11) March 20, 2000, the Company announced that they would restate earnings.
(12) July 7 1999, the Company substantially reduced their earnings expectations as a result of prior material misrepresentations to analysts and the investing community.
(13) April 15, 1998 the Company announced accounting problems.
(14) July 27, 2001 investors file a lawsuit against the Company alleging false and misleading statements.
(15) April 30, 2002, first class action complaint was filed alleging accounting fraud by WorldCom and CEO resigns. Additionally, since the price 7 days after the announcement was made was unavailable, a stock price of zero was used, as the Company filed for bankruptcy shortly after the announcement (July 21 2002). See chart below for more detail.
(16) October 12, 2001 the Company announced that it made a US \$638 million loss during the third quarter of the fiscal year 2001.
(17) January 14, 2002, investors and analysts express concerns about accounting disclosures in the wake of Enron. The Company did not launch an investigation into the executive loans until June 6, 2002, after the CEO's indictment for tax evasion. Since the stock dropped substantially due to accounting concerns before the investigation, the January 14, 2002 date is used. Additionally, the 7 days subsequent to the announcement of the results of the internal probe will be used as the "7 day Price After Announcement."
(18) May 6, 2002, the Company announced a restatement.
(19) April 28, 1999, the Company issues a press release stating that they will need to restate results.
(20) April 3, 1998 the Company issued a press release stating that they would miss first quarter earnings

Shareholder losses based on date of last unquestioned SEC filing

Table A2 examines the decline in total market capitalization for the period beginning on the date of the last unquestioned SEC filing through the period of resolution. The date of the last unquestioned filing is the date of the quarterly or annual filing immediately preceding the announcement of a problem. The resolution date is that date when investors received information resolving uncertainty about the accounting issue. Often the registrants filed amendments to restate their previously issued financial statements. In other instances, the registrants made public announcements indicating that they would restate, including quantitative information about the restatement. The time period corresponds to the interval beginning on the date when information based on original financial statements is most likely to be incorporated in market prices. This time period is likely to capture the economic effect of the market's reaction to the restatement event. It may, however, also capture the effect of other factors that may be indirectly related to or unrelated to the restatement. For example, the resignation of a CFO, director or auditor may occur or a lawsuit may be filed during this time period. Results indicate that over the long-term, accounting problems substantially impact stock prices.

Table A2: Market Cap Declines from Date of Last Unquestioned Filing Date Prior to Disclosure through Resolution

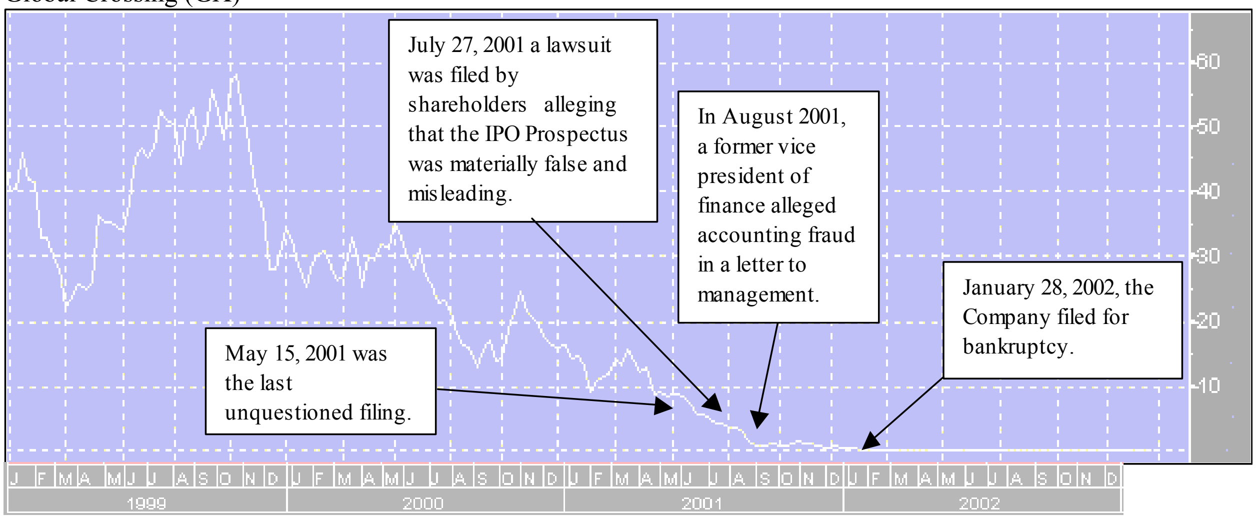
Company Name	Ticker	Last Unquestioned Filing Date	Resolution Date	Lost Market Cap ($ in millions)	Cumulative Return
Global Crossing (1)	GX	5/15/01	bankrupt	(11,689.7)	-100%
Krispy Kreme (2)	KKD	4/16/04	Not yet resolved	(1,576.5)	-78%
Critical Path (1)	CPTH	11/14/00	bankrupt	(2,710.9)	-100%
Network Associates	MFE	11/14/00	12/26/00	(335.5)	-13%
Rite Aid	RAD	7/13/99	10/11/00	(5,550.3)	-88%
Lernout & Hauspie (1)	LHSP	3/31/00	bankrupt	(5,183.3)	-100%
Symbol Technologies (1)	SBL	11/2/01	bankrupt	(3,001.0)	-100%
Health South (3)	HLSH	8/14/02	8/27/02	(2,256.5)	-50%
Oxford Health Plans	OHP	8/5/97	4/3/98	(5,057.5)	-79%
Adelphia (1)	ADELQ	11/15/01	bankrupt	(3,933.6)	-100%
MicroStrategy	MSTR	1/28/00	6/22/01	(11,859.4)	-98%
Waste Management	WMI	5/14/99	12/20/99	(24,418.2)	-73%
Cendant	CD	3/31/98	10/13/98	(24,442.7)	-73%
Qwest	Q	5/15/01	11/8/04	(55,685.0)	-89%
WorldCom (1)	WCOM	3/13/02	bankrupt	(19,969.5)	-100%
Enron (1)	ENE	8/14/01	bankrupt	(32,090.2)	-100%
Tyco	TYC	12/28/01	12/31/02	(80,857.6)	-70%
Peregrine Systems (1)	PRGN	11/4/01	bankrupt	(3,253.4)	-100%
McKesson HBOC	MCK	4/22/99	7/14/99	(9,097.5)	-51%
Sunbeam (1)	SOC	1/29/98	bankrupt	(3,079.1)	-100%
	TOTAL			(306,047.5)	-80%

Source: GLC, Capital IQ, and BigCharts.com Note: Company's in the above table were selected based on the large market capitalization changes associated with their accounting announcements. The data is not adjusted for other market changes occurring during the respective time periods affecting each firm.
(1) In instances where a company declared bankruptcy, the stock price at the resolution date is assumed to be zero.
(2) The resolution date reflects the closing stock price on April 11, 2004, as the accounting issues have not yet been resolved
(3) The resolution date reflects the closing stock price on April 11, 2004, as the accounting issues have not yet been resolved
(4) The press release date was used as the resolution date since the Company took an abnormal amount of time to file an amended 10-K.

Individual Stock Charts

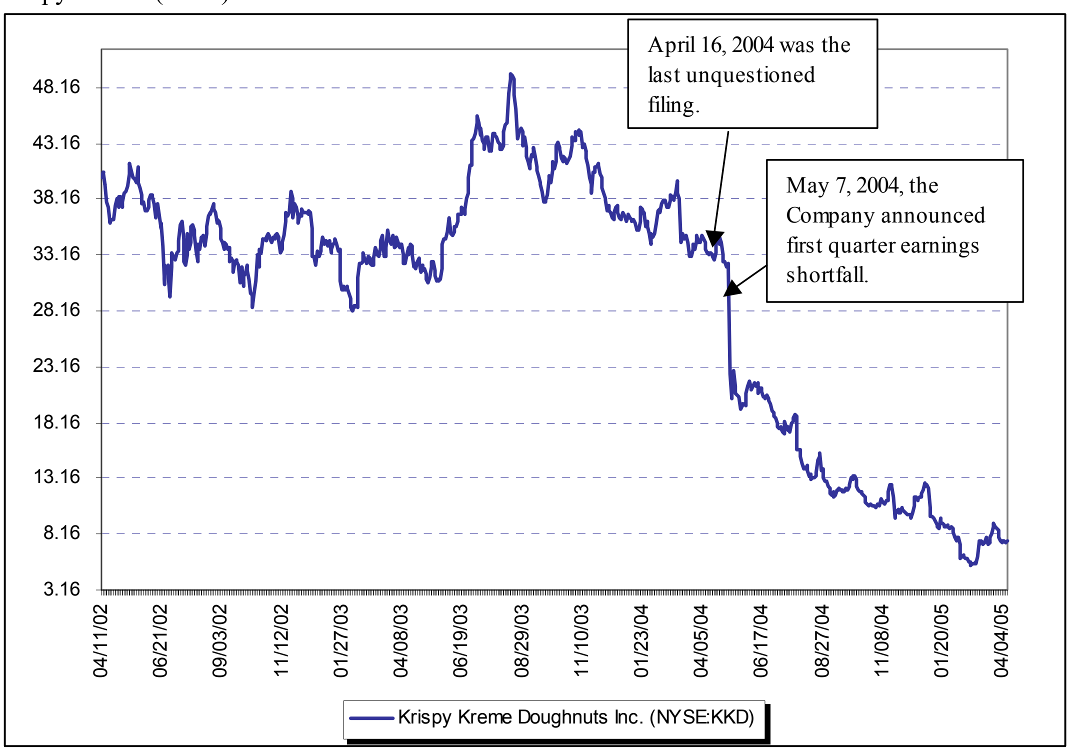
The following are individual stock charts for the companies in Table A1 and A2 above. These charts provide detail surrounding the events that lead to a price decline in the stock including, the last unquestioned filing date, company press releases and articles, and the resolution dates (i.e. date of the filing of the amended 10-K.)

Global Crossing (GX)



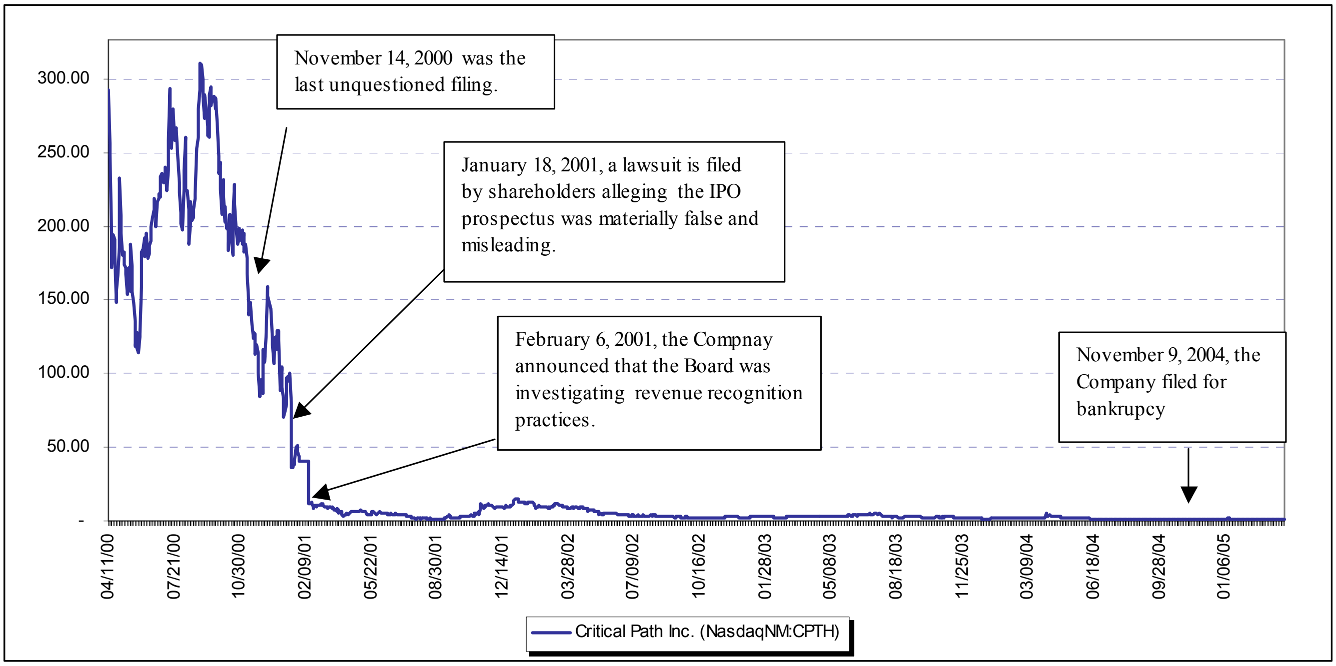
Source: Bloomberg.

Krispy Kreme (KKD)



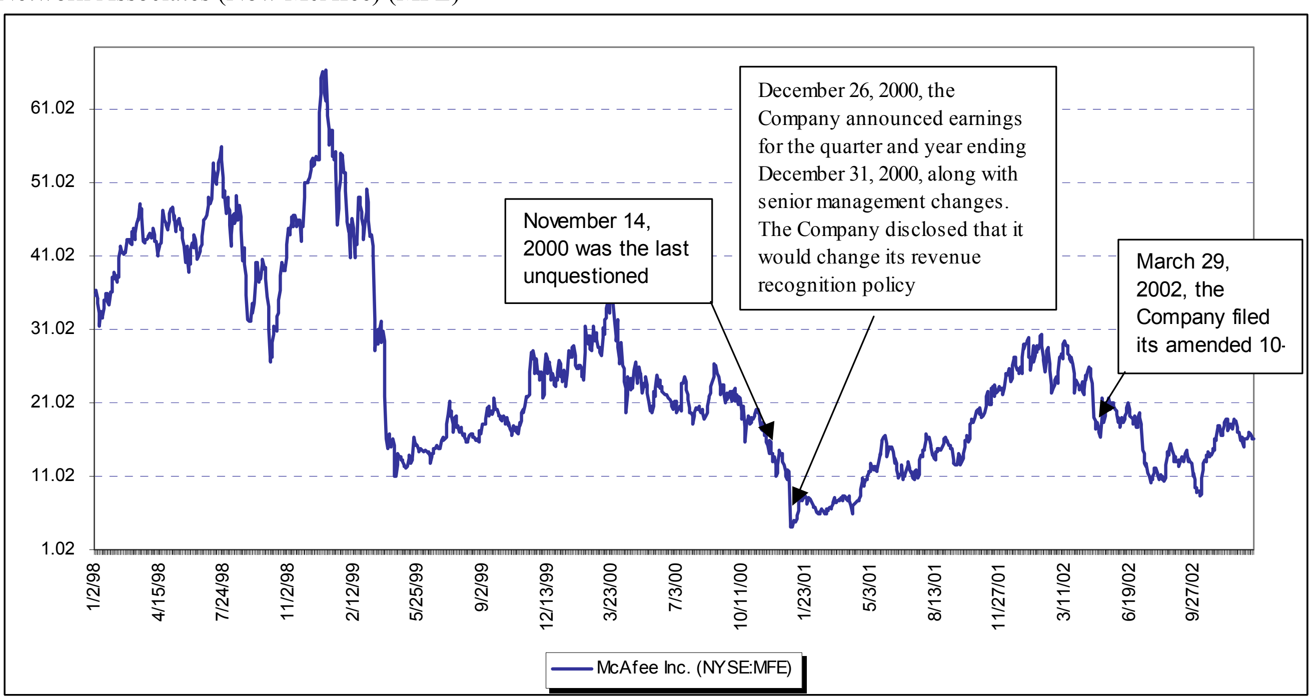
Source: GLC, Capital IQ.

Critical Path (CPTH)



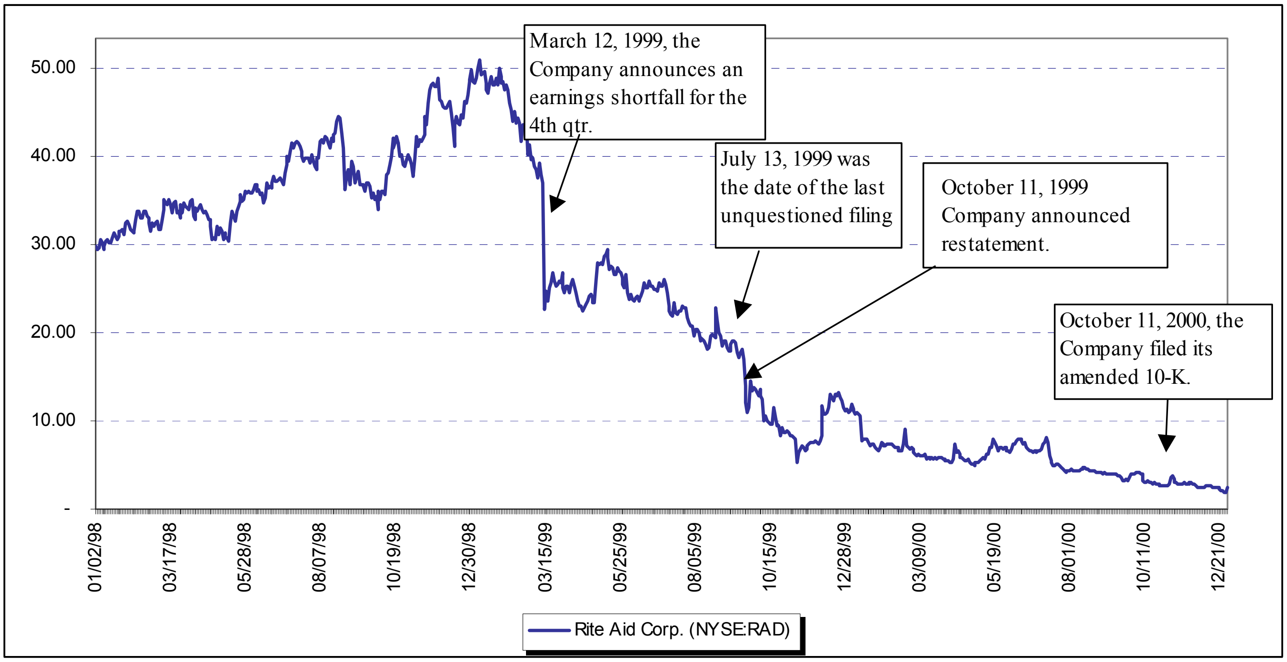
Source: GLC, Capital IQ.

Network Associates (Now McAfee) (MFE)



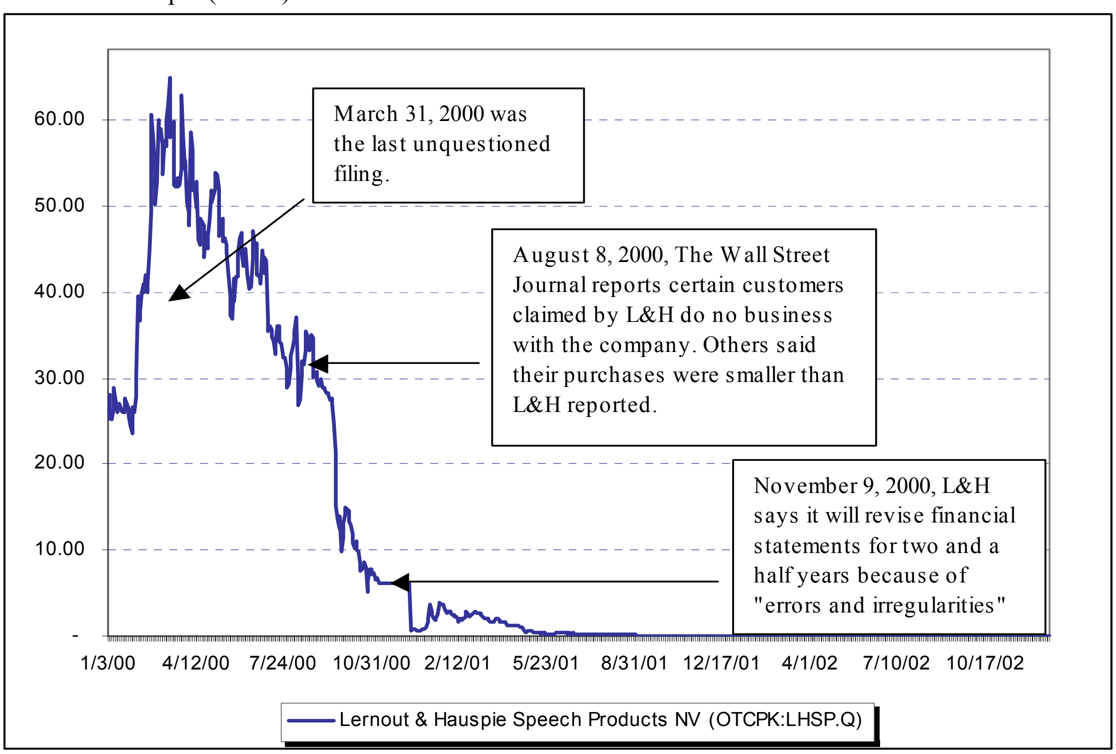
Source: GLC, Capital IQ.

Rite Aid (RAD)



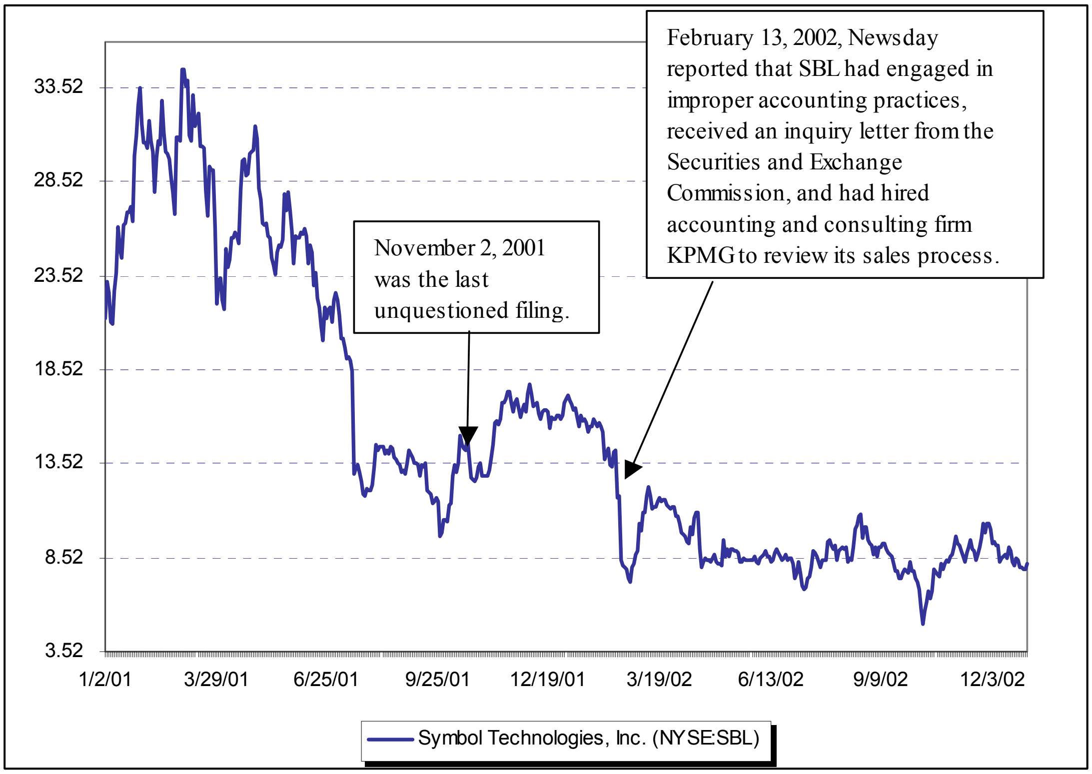
Source: GLC, Capital IQ.

Lernout & Hauspie (LHSP)



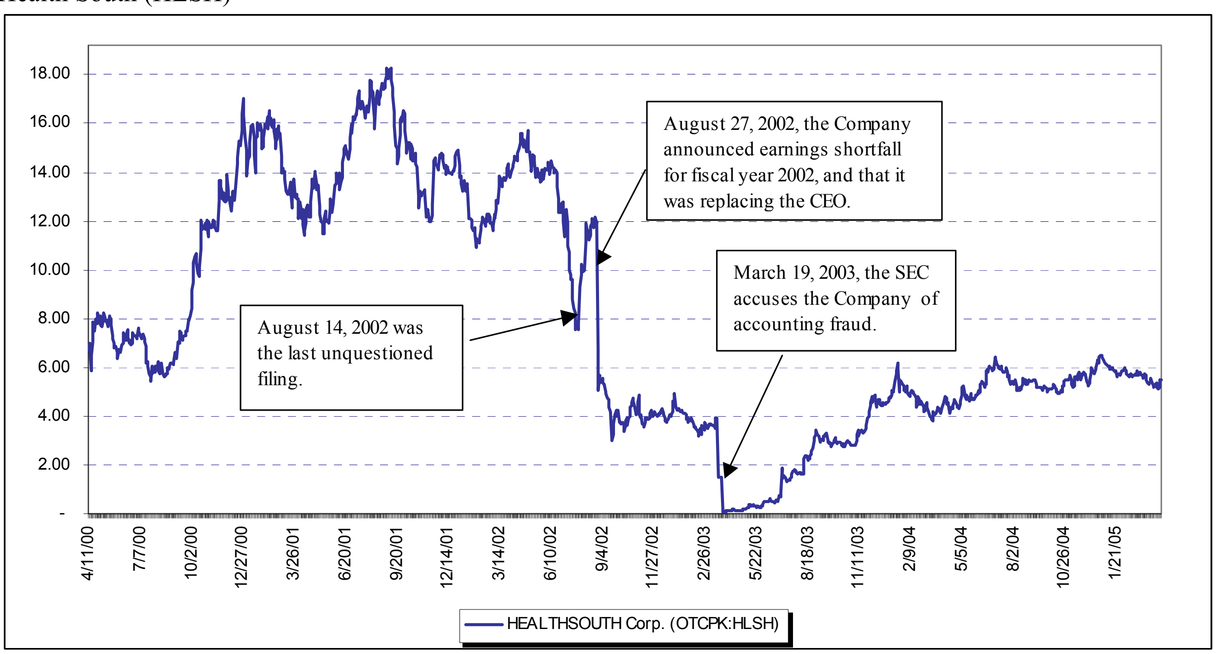
Source: GLC, Capital IQ.

Symbol Technologies (SBL)



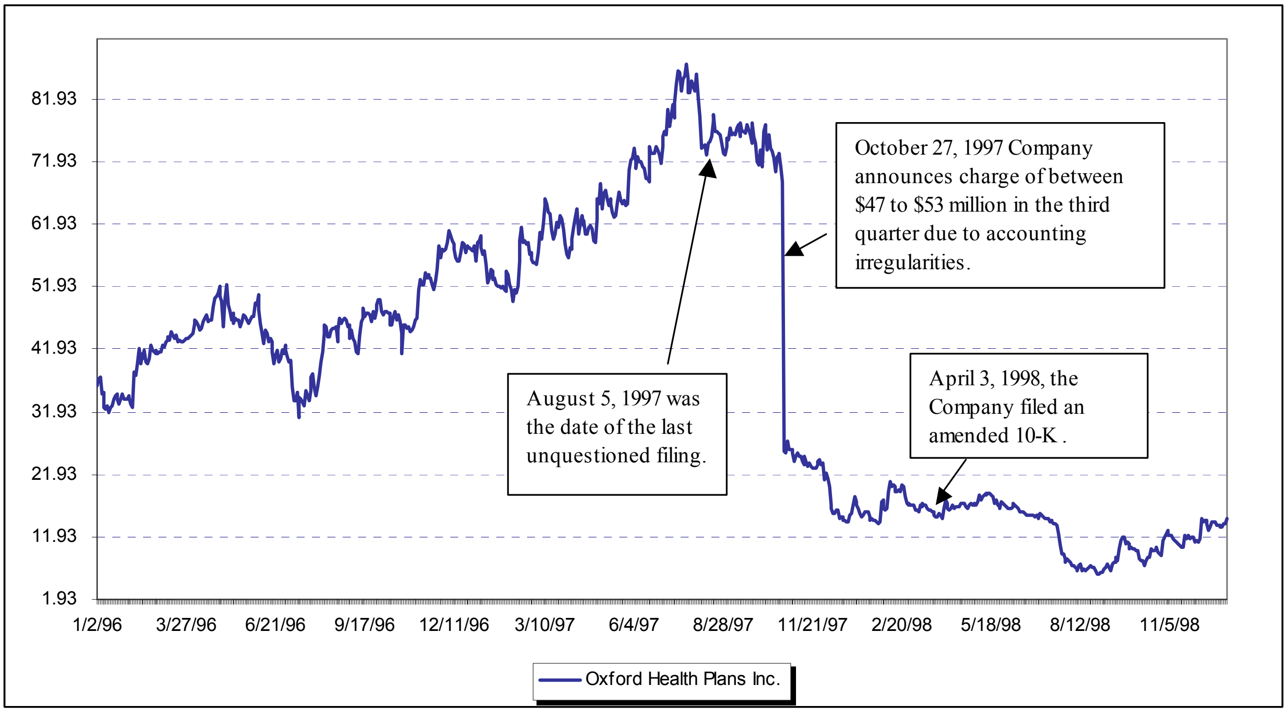
Source: GLC, Capital IQ.

Health South (HLSH)



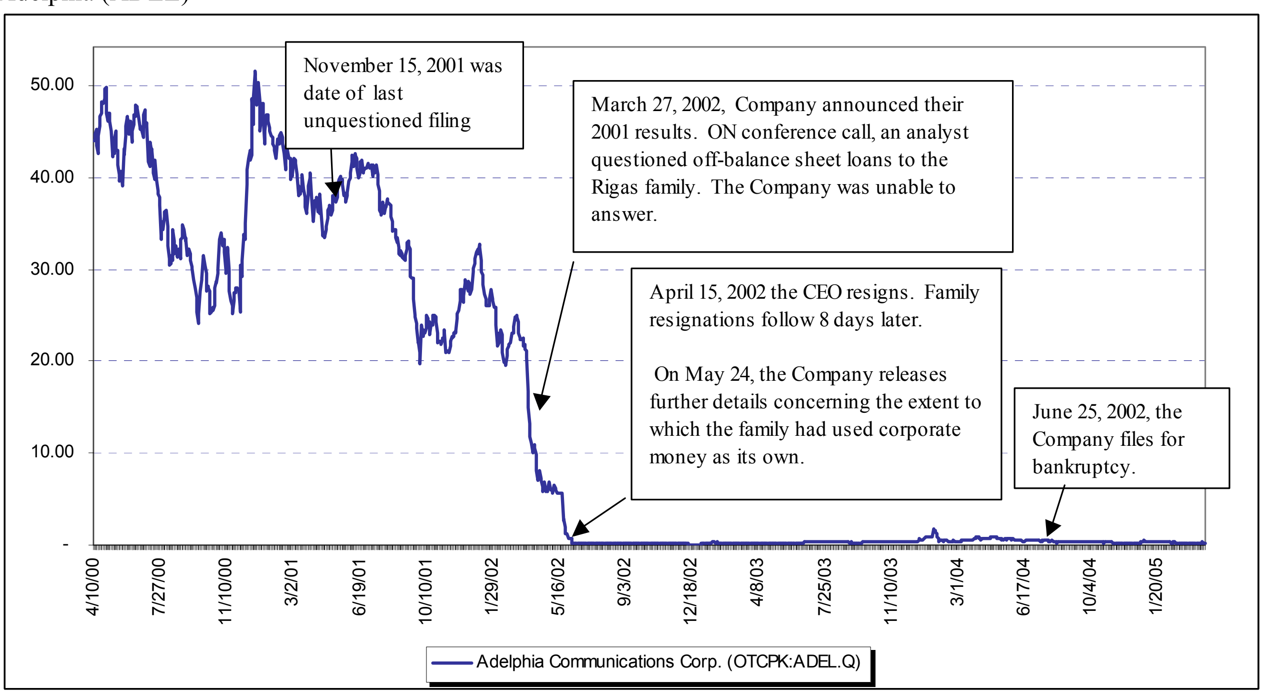
Source: GLC, Capital IQ.

Oxford Health Plans (OHP)



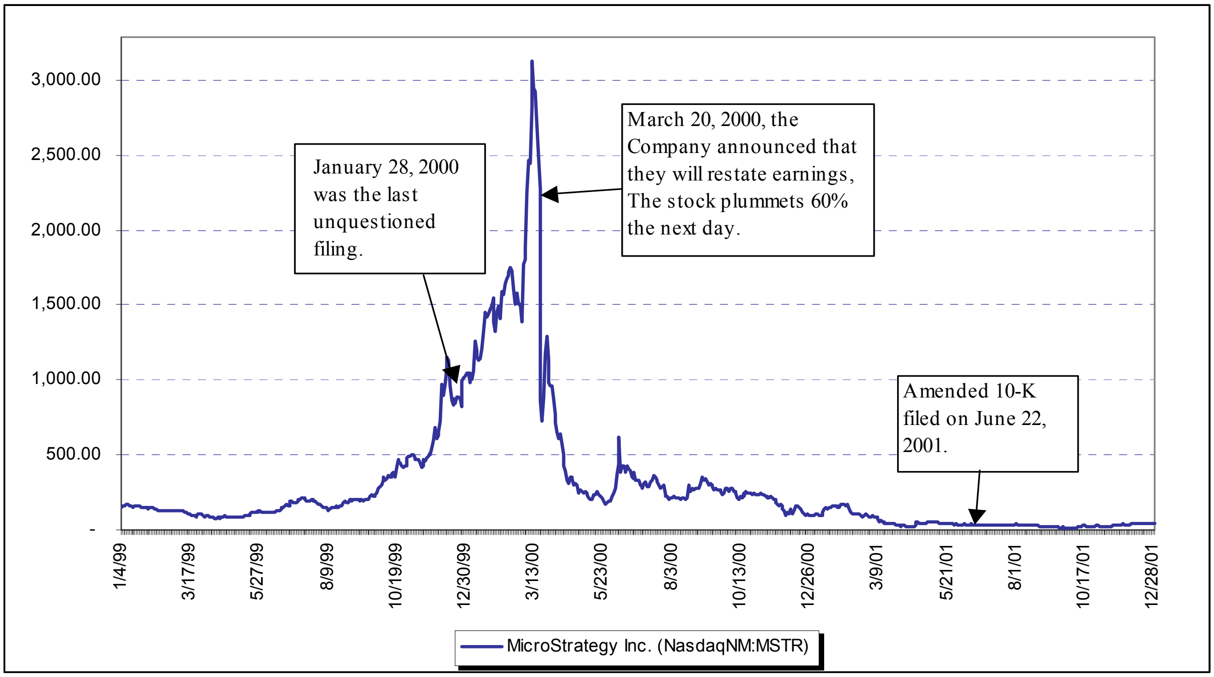
Source: GLC, Capital IQ.

Adelphia (ADEL)



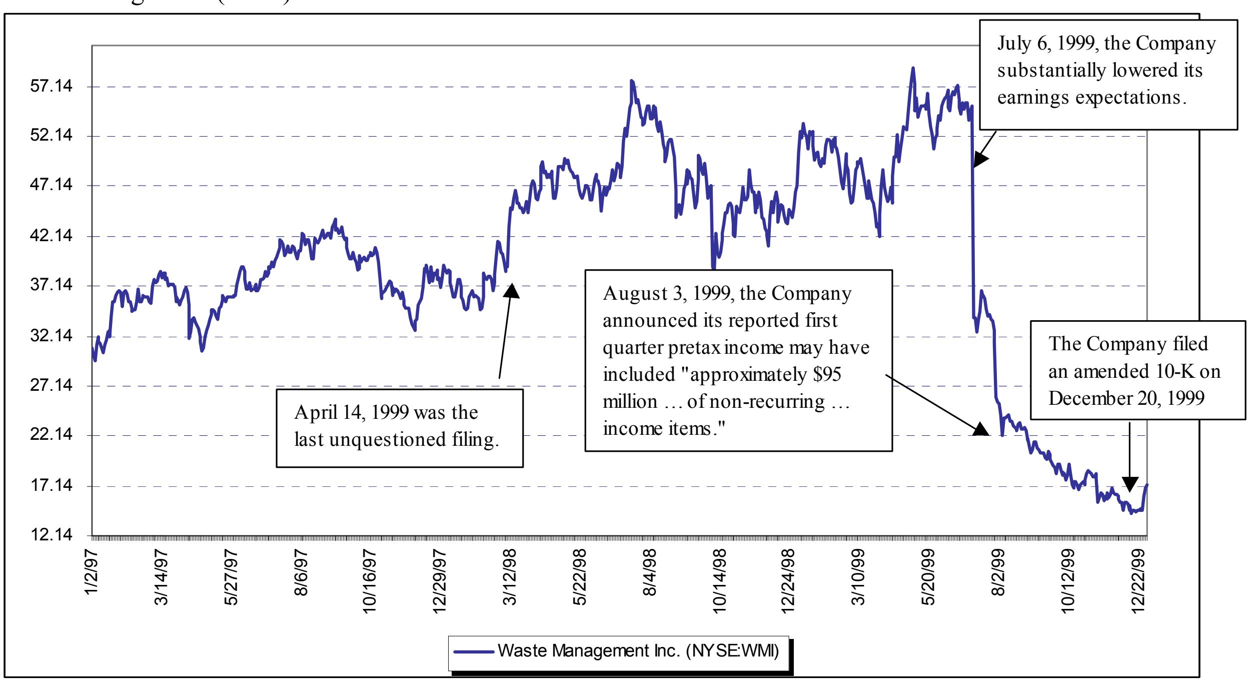
Source: GLC, Capital IQ.

MicroStrategy (MSTR)



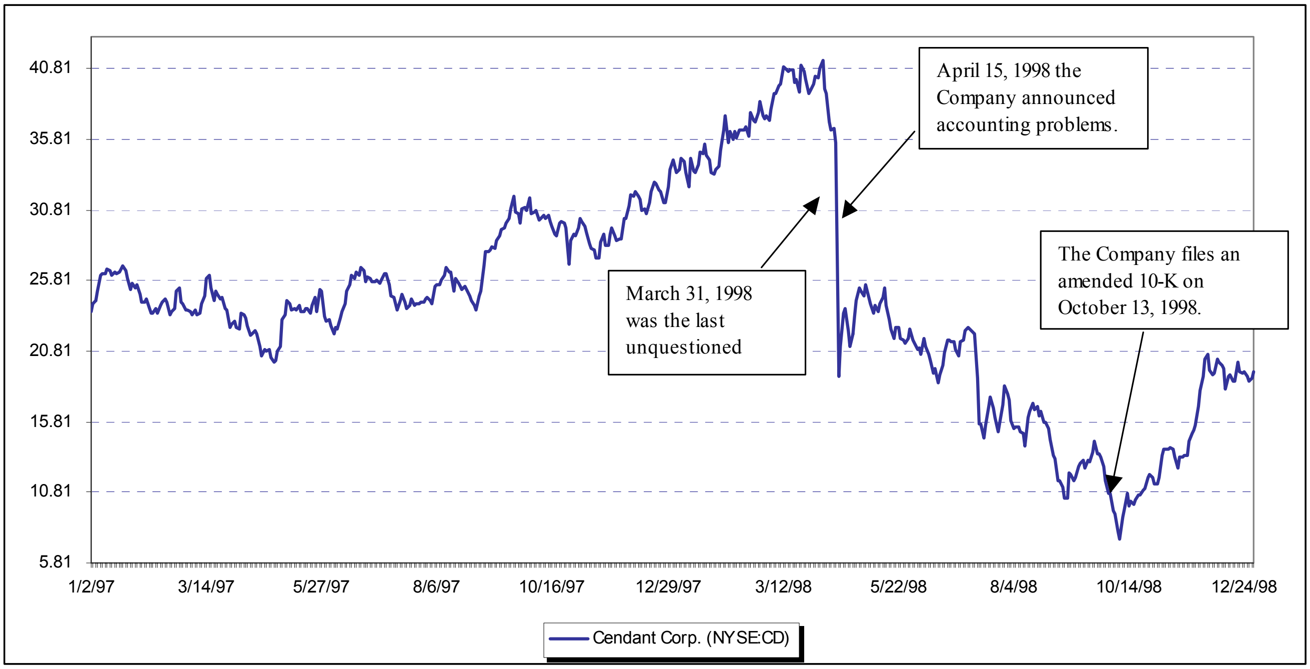
Source: GLC, Capital IQ.

Waste Management (WMI)



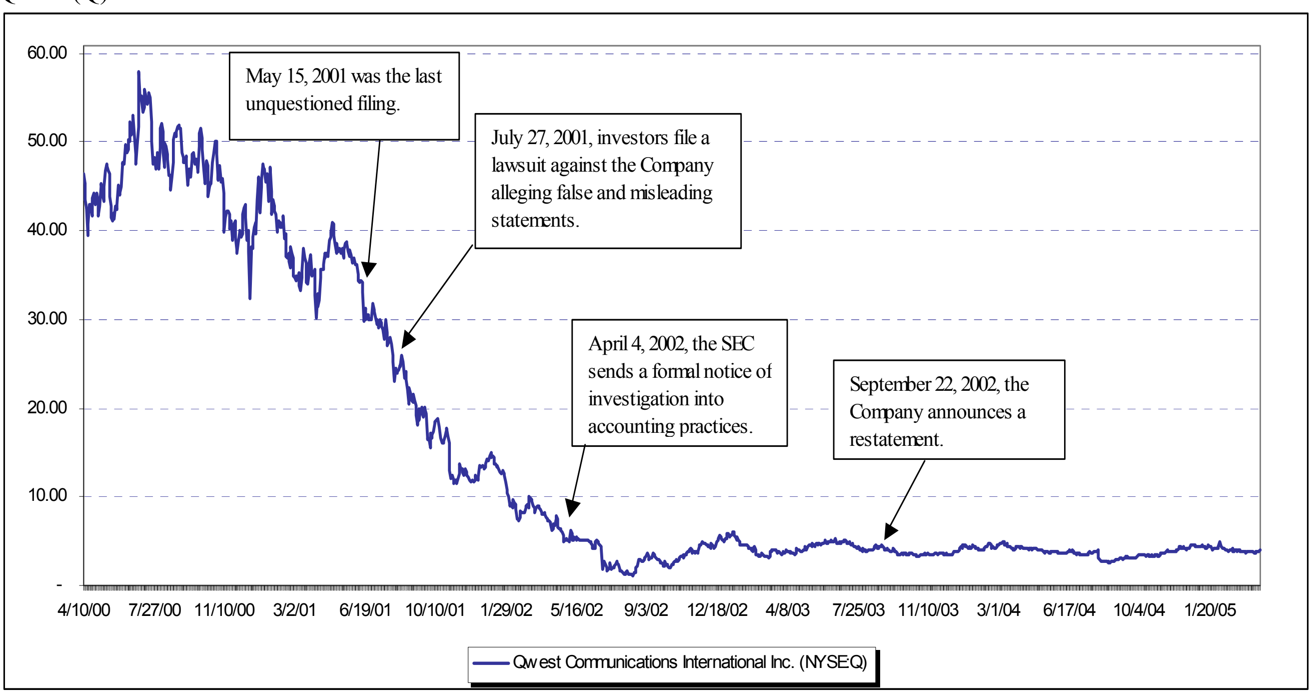
Source: GLC, Capital IQ.

Cendant (CD)



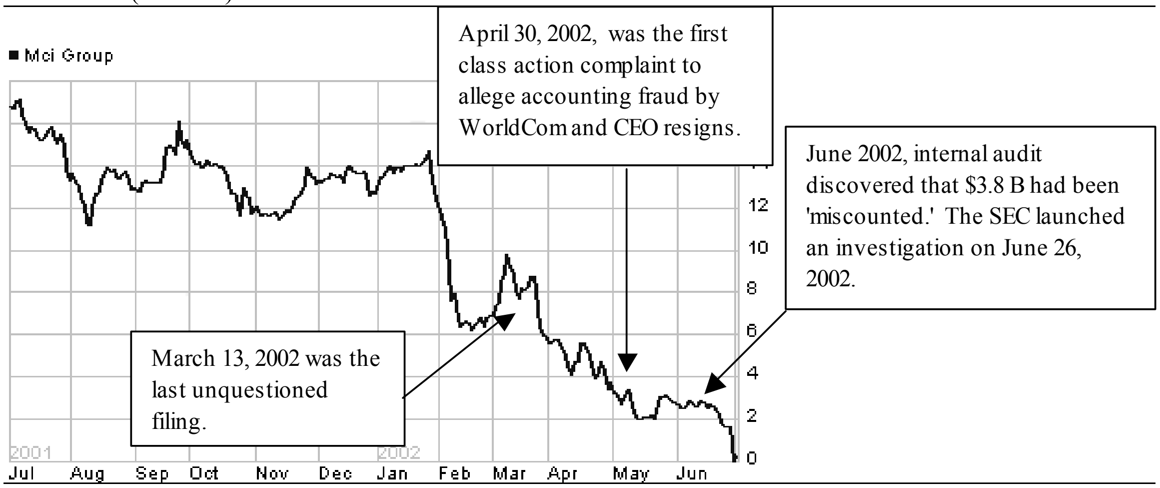
Source: GLC, Capital IQ

Qwest (Q)



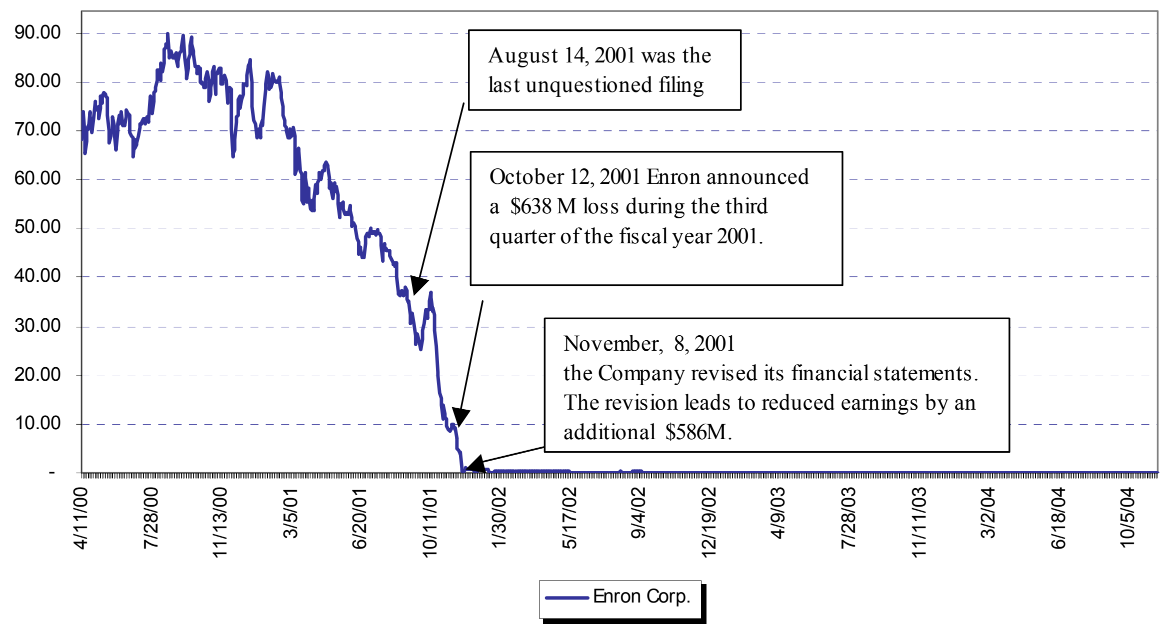
Source: GLC, Capital IQ.

WorldCom (WCOM)



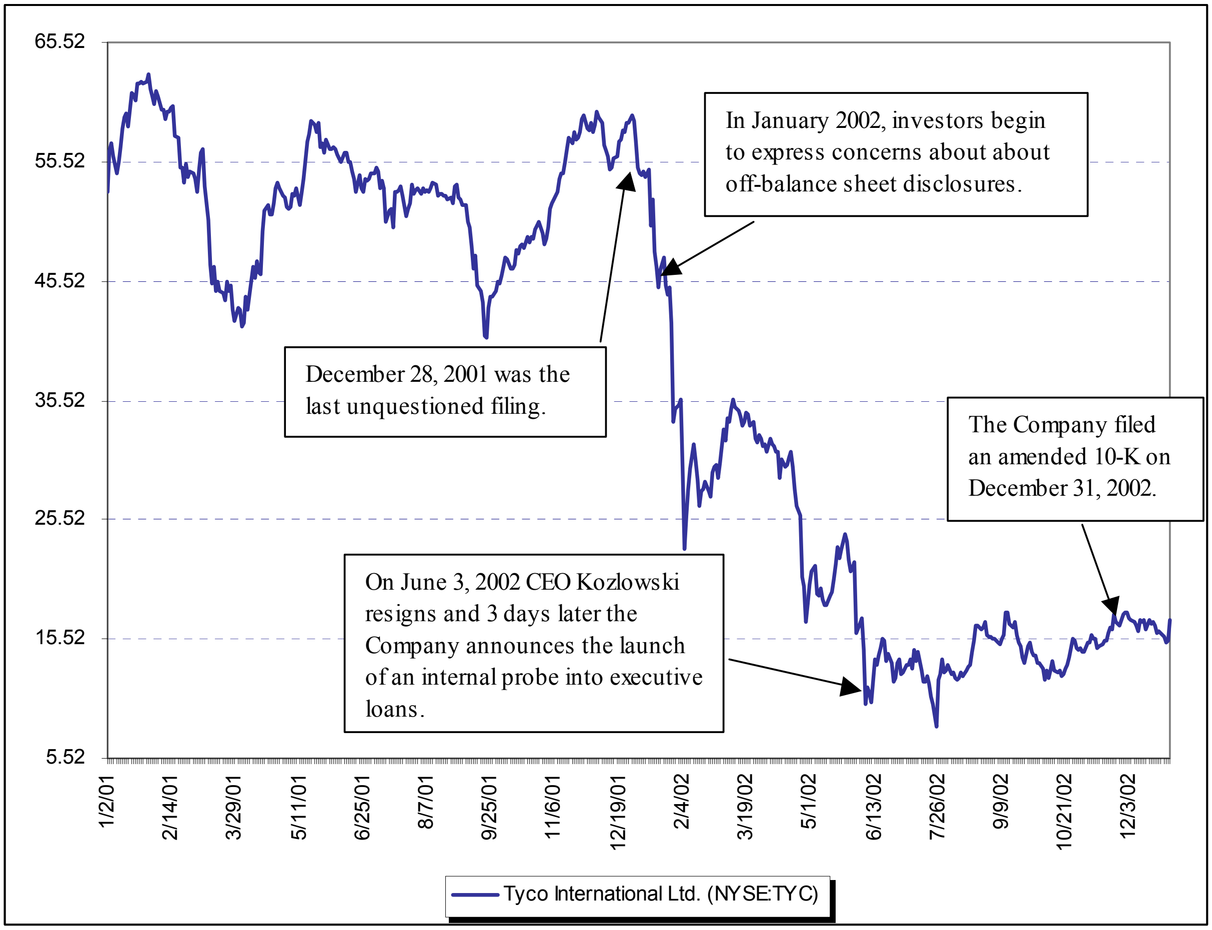
Source: BigCharts.com.

Enron (ENE)



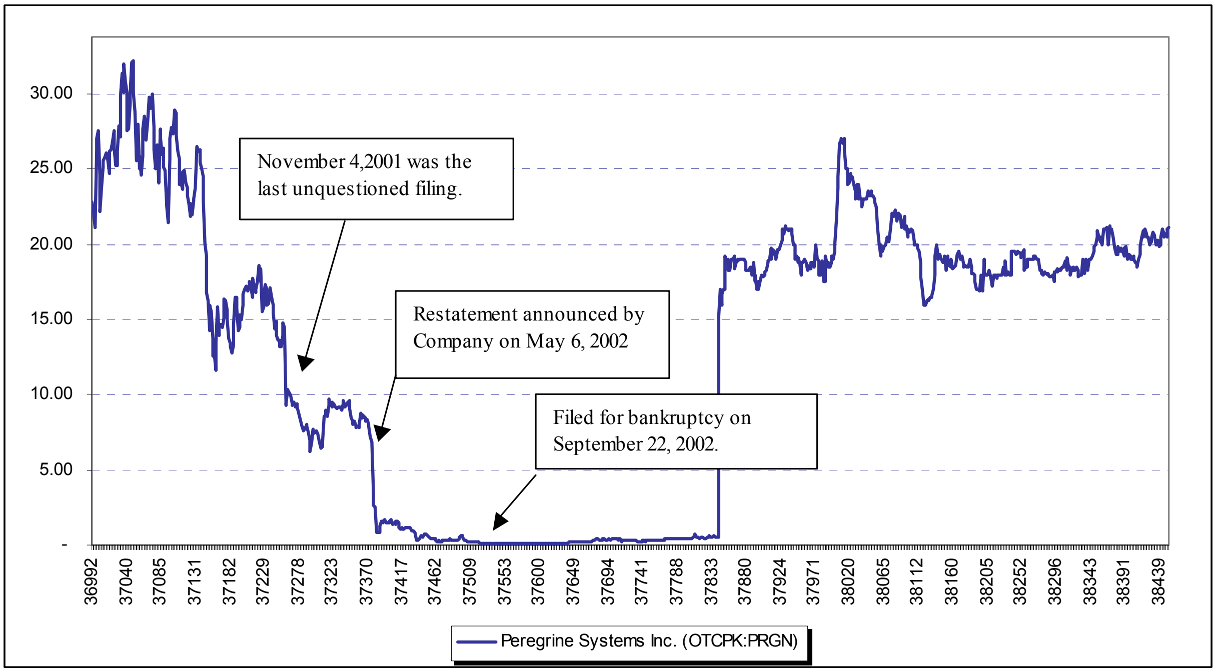
Source: GLC, Capital IQ.

Tyco (TYC)



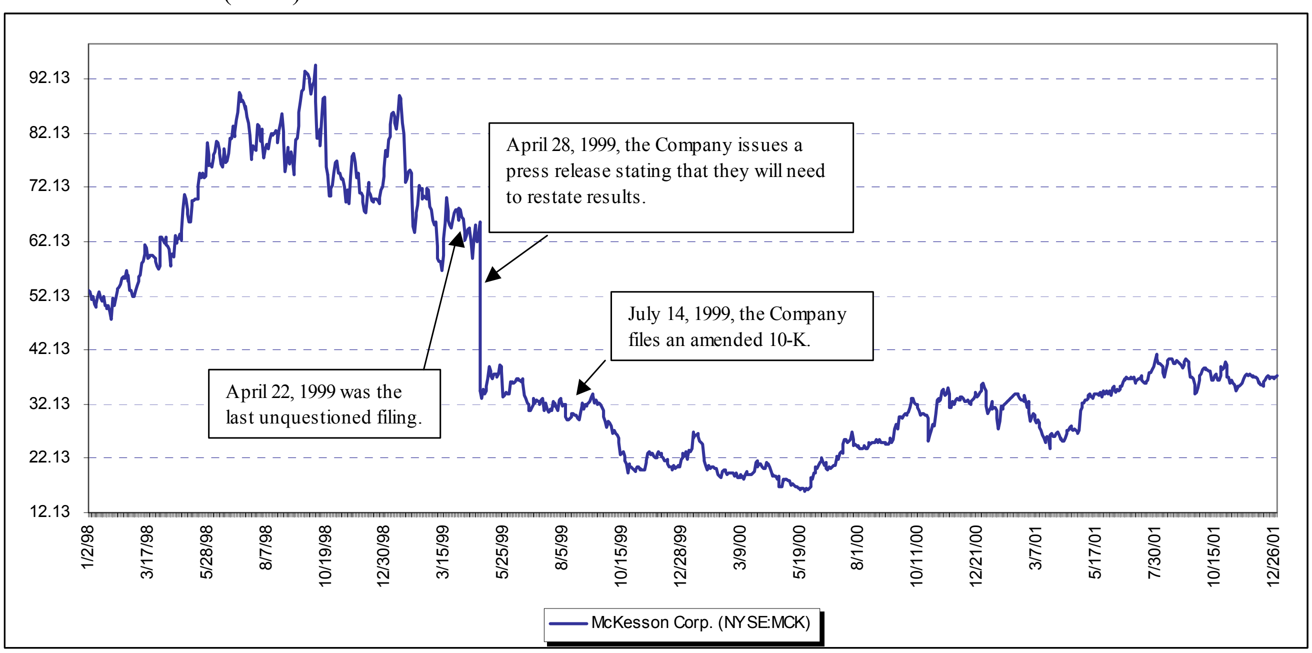
Source: GLC, Capital IQ, Wall Street Journal.

Peregrine Systems (PRGN)



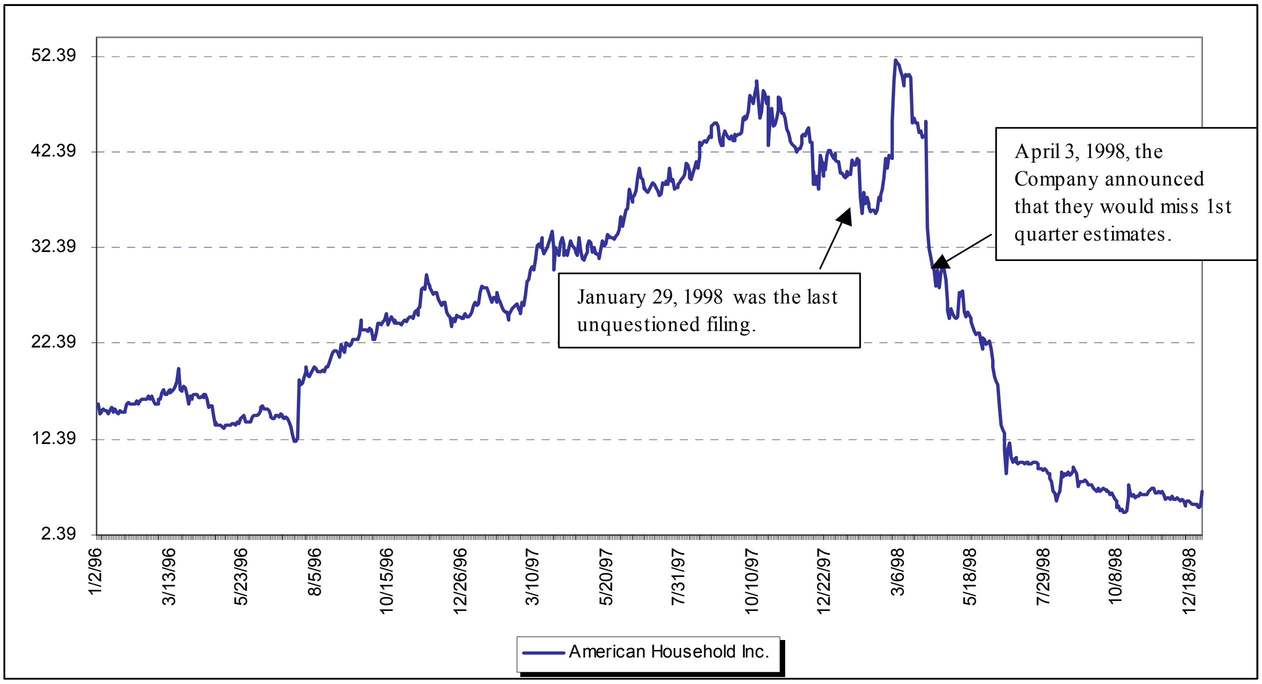
Source: GLC, Capital IQ.

McKesson HBOC (MCK)



Source: GLC, Capital IQ.

Sunbeam (SOC)



Source: GLC, Capital IQ.

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