

RECORD OF PROCEEDINGS

SECURITIES AND EXCHANGE COMMISSION

ADVISORY COMMITTEE
on
SMALLER PUBLIC COMPANIES

October 14, 2005

1:00 p.m.

Columbia Law School
Jerome Green Hall
435 West 116th Street
New York, New York

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PROCEEDINGS

The following Members were present in person:

Patrick C. Barry

Joseph "Leroy" Dennis

Robert E. Robotti

Kurt Schacht

James C. Thyen

Herbert S. Wander

The following Members were present by telephone:

Steven E. Bochner

Richard D. Brounstein

C.R. "Rusty" Cloutier

Alex Davern

Janet Dolan

Mark Jensen

Richard Leisner

The following Members were absent:

Pastora Cafferty

James A. "Drew" Connolly

E. David Coolidge

Richard M. Jaffee

Deborah Lambert

Scott Royster

Ted Schlein

John Veihmeyer

The following Official Observers were present by telephone:

Daniel L. Goelzer

Jack E. Herstein

The following Official Observer was absent:

George Batavick

The following SEC staff were present in person:

Gerald J. Laporte

Kevin M. O'Neill

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MR. WANDER: I would like to call this meeting of the SEC Advisory Committee on
Smaller Businesses to order and thank all of our guests who are here in person and members of
the committee who are here, and also to Columbia Law School for their very gracious
hospitality, as they did earlier this year in June.

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Before we go into any business and make any introductions, I think it is appropriate to
have a roll call since this meeting is being webcast and many members of the Advisory
Committee and the Advisors are on the telephone. So I will go down the list of members of the
committee and observers and ask for you to indicate your presence if you are.

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First is Pat Barry who is here in person.
George Batavick is not available.
Steve Bochner?
Richard Brounstein?

1 MR. BROUNSTEIN: Yes, Rick is here.

2 MR. WANDER: Hi, Rick.

3 Pastora Cafferty?

4 Rusty Cloutier?

5 MR. CLOUTIER: Yes, I am here.

6 MR. WANDER: Hi, Rusty, hope all is going well down in Louisiana.

7 MR. CLOUTIER: Things are slowly getting back to normal.

8 MR. WANDER: Drew Connolly? I know he is on a plane someplace I believe.

9 Dave Coolidge?

10 Alex Davern?

11 Leroy Dennis is here in person.

12 Janet Dolan?

13 MS. DOLAN: Yes.

14 MR. WANDER: Dan Goelzer?

15 MR. GOELZER: Yes, here by telephone.

16 Jack Herstein?

17 MR. HERSTEIN: Present by phone.

18 MR. WANDER: Dick Jaffe?

19 Mark Jensen?

20 MR. JENSEN: Here on the phone.

21 MR. WANDER: Debbie Lambert?

22 Richie Leisner?

23 Bob Robotti?

1 Scott Royster?

2 Kurt Schacht is here, right, Kurt.

3 Ted Schlein?

4 Jim Thyen?

5 MR. THYEN: Here.

6 John Veihmeyer?

7 And Herb Wander is here.

8 MR. BOCHNER: And Steve Bochner joined too.

9 MR. WANDER: Oh, hi, Steve. Thank you.

10 In addition, from the SEC staff, we have Gerry Laporte and Kevin O'Neill in person. I
11 think that's everyone.

12 As many of you know, we have had a number of hearings, Columbia in June, Chicago in
13 August and San Francisco in September, at which time a number of parties presented their
14 positions in a roundtable fashion similar to what we will do this afternoon to provide advice and
15 guidance to the Advisory Committee on calibrating the regulations dealing with smaller public
16 companies. And those people who have testified have been corporate executives, chief financial
17 officers, accountants, investors, analysts. I think that covers almost -accountants, everybody
18 across the wide spectrum of people who are very interested in corporate governance and the
19 disclosure regulations and the regulatory regime of the securities laws. Today, we are having an
20 extra session to focus on really investors' views, small cap investor views of the effects of the
21 securities regulation, and in particular, Sarbanes-Oxley, and in special emphasis Section internal
22 controls on smaller public companies. I think it's also appropriate at this time to mention to you

1 as a sort of working definition, the subcommittee has accepted the views of our definition
2 committee, size definition committee, and for practical purposes --

3 MR. DAVERN: Alex Davern here.

4 MR. WANDER: Hi, Alex.

5 MR. DAVERN: Hi, how are you doing?

6 MR. WANDER: Good. We have already started and glad to have you.

7 MR. DAVERN: Glad to be here.

8 MR. WANDER: We have defined, for our working purposes, smaller public companies
9 as those essentially in the bottom six percent of the aggregate of market capitalization, which
10 really becomes all the public companies under that WKSI, which is the new definition adopted
11 by the SEC as part of their Securities Act reform. And that essentially is companies , million of
12 total market cap. We have further divided it below that number.

13 MR. WANDER: Hello?

14 MR. LEISNER: Herb?

15 MR. WANDER: Yes.

16 MR. LEISNER: It's Richie Leisner.

17 MR. WANDER: Hi, Richie. Thank you for joining us. We are already sort of in -- we
18 are already in progress. And we have further divided the companies into micro caps, which is the
19 bottom one percent of total market capitalization. And essentially those are companies under , ,
20 maybe even million because it slides. I think that's the background that I would like to have for
21 our meeting today. This is probably the last meeting where we will hear oral presentations,
22 although you never know, things change and if things become important on our agenda where we
23 need additional information, I guess we could schedule some other meetings, but as of now, this

1 is the last one. Although, I do urge everyone who is listening who is interested who haven't
2 provided the committee with their views, I think we will still accept your written views on any of
3 the subjects that are before our committee because we find these written views very helpful. The
4 answers to our questionnaires, we've gotten -some questionnaires back on questions and even
5 though it took a week or so to read them all, I think they have been extremely helpful. What
6 would like to do now, unless there is any other business, Jim?

7 MR. THYEN: No. Let's proceed, Herb.

8 MR. WANDER: We do have present, I should say, Pat Barry, Kurt Schacht, Leroy
9 Dennis, Jim Thyen and myself from the Advisory Committee in person.

10 Our first panel consists of three representatives of primarily investors: Tom Russo, Tom
11 Duncan and Jane Adams. In the past rather than me give long introductions, we thought it would
12 be appropriate if you introduced yourselves and told us a little bit about yourselves and then
13 made a presentation, and then members of the Advisory Committee and our observers will ask
14 you some questions and you can also ask each other questions or make comments after you've
15 heard the presentations of the other presenters. So, Tom, let's start with you, and many thanks
16 for your participation.

17 MR. RUSSO: My pleasure. Let's see, I am what you would call -- in the investment
18 world, I am in the camp of value investor. I manage funds for largely taxable investors with a
19 long-term buy and hold bias. I and my colleagues invest nearly \$3 billion and we are both
20 prepared to invest in foreign and U.S. companies, so we have quite a background in investing in
21 non-U.S. companies as well as U.S. companies. And we have investments in smaller companies
22 as well as larger companies, so our experiences would sort of align with what you are looking for
23 advice on. Then as a professional, I came from Stanford Business and Law School and have had

1 the pleasure of spending time with former Commissioner Joe Grundfest through his Director's
2 College, so lots of these issues have come up over the past five years as I have attended that,
3 so...and that's my way of introduction. I am pleased to participate.

4 MR. WANDER: Would like to make a presentation to us?

5

6 MR. RUSSO: Well, I think there are a variety of points. I do have, specific to Section
7 404 as it relates to smaller companies, on behalf of investors I have a position in one such
8 company something like 12 percent of their outstanding shares. I know the company well. It is a
9 global paper company. And the comments that they have made about the costs of the
10 compliance with the Sarbanes-Oxley audit and the difficulties they encountered are clear. They
11 passed with no discoveries, they passed both levels, and, yet, the thing -- it came at quite a
12 considerable amount of expense and distraction.

13 And what they are concerned over is, first, that they will have to do it next year, that it is
14 a continuous process. And so they would believe that the second, third and following years for a
15 firm that has had no transgressions and with internal controls unchanged ought to recognize the
16 first year's success and, hopefully, face a different requirement following years. That's the first
17 time point made.

18 The second point made was that there seems to be lacking implementing guidance from
19 the PCAOB, no willingness on the part of their auditors to apply any kind of judgment in
20 implementing the audit for Sarbanes-Oxley, and so, unlike in financial audits where there is a
21 materiality test which allows the auditor some degree of judgment, it's unclear what latitude the
22 auditors have in this area. And absent that, their tolerance is zero in effect and it leads to
23 enormous amounts of cost and expenses. I guess as an observation, it would have, and I have
24 heard this through many companies, it would have driven a wedge between the relationship that

1 has existed between auditors and their public companies over time because of the inability for
2 the auditors to have any kind of role in this particular Section compliance audit that has room for
3 judgment.

4 Those are two things that I would stress. First, the continuous nature, and, second, the
5 lack of ability for the auditors to exercise judgment. Those are the two highlights that I would put
6 before you.

7 MR. WANDER: As an investor in a wide variety of the securities, \$3 billion under
8 management, are there any other aspects of Sarbanes-Oxley or securities regulation that you
9 think the committee should address, particularly in terms of smaller public companies?

10 MR. RUSSO: Let me come back to that. I was focused, at least initially, on this
11 narrower point. But having that offered for comment, I am going to think about it and come
12 back, but I don't want to speak prematurely, but, please, let me come back to that.

13 MR. WANDER: Sure. Questions from the Advisory Committee? Leroy?
14

15 MR. DENNIS: Leroy Dennis. Have you -- has your company received any estimates of
16 what they expect those costs to be in the future? We have heard a variety of estimates come out.

17 MR. RUSSO: Yeah, I had a very specific conversation in this case, and it was a million
18 and a half dollars of incremental audit. It was 6 cents a share in terms of this company's earnings
19 per share because of the relatively small nature of the company.

20 MR. WANDER: 6 of what?
21

22 MR. RUSSO: 6 cents per share of earnings.
23

24 MR. WANDER: Of what were the earnings, so we can --
25

26 MR. RUSSO: Basic maybe \$2, so it is a 3 or 4 percent order of magnitude. But that is
27 after they engaged their auditors with some pressure, because it was their opinion, I think it's

1 shared across all of the companies that I have heard from, that the burden on the industry to audit
2 Sarbanes-Oxley has led to hiring of an enormous number of new auditors, many from foreign
3 countries that have challenges with the English language, and so the yield from the people who
4 actually were involved with this was quite low. So they are still out a million and a half dollars,
5 but only after they forced the bill down for lack of effectiveness on many of those hours billed.
6 So that's the first thing.

7 So that's the direct cost of a small company is quite high. A special note that in smaller
8 companies, very often the senior executives own a lot of stock, and they really do begrudge
9 writing those checks because it is their money at the same time. And I think you find that to be
10 true across many of the smaller companies.

11 The second area I have heard expressed as a concern is the area of distraction, the costs of
12 distracting management, especially when you take the test down to zero tolerance and they have
13 no auditor room for judgment. It's just the inexorable amount of distraction and costs for a small
14 and lien managed company.

15 And then the third area of cost is separate from the auditor's cost but it was expressed by
16 a larger company, Silicon Valley, where they had \$7 billion market cap and they had 400
17 different divisions or controls audited. We are dealing with \$10,000, oversight, so in order of
18 magnitude, quite a small error on their systems part. But what they expressed is that now that
19 they have audited those 400-plus different controls, that if somebody in their company came up
20 with a new product or a new route to market it, a new controlled unit, they would wait just a
21 second to see whether they should implement it because it may burden the process. And it is the
22 lack of willingness to set forth on a new business in this case that would actually be the biggest

1 cost, if, in fact, it's so, because the burden placed on them for controlling such new enterprise is
2 too high.

3 MR. DENNIS: Herb, may I?

4 MR. WANDER: Sure.

5 MR. DENNIS: Thank you. How big -- the company that you have, does it fit into our
6 micro cap definition?

7 MR. RUSSO: The first one absolutely does. I think it has 11 million shares outstanding
8 and it has a \$22 market price, so that's \$220 million. It's global and so it's unusual from that
9 standpoint.

10 MR. DENNIS: My question to you is really as an investor. We all know the cost of
11 Sarbanes and it's been a lot more than what we all originally thought it was going to be, but as an
12 investor with money to invest in small companies, a company that did a lesser amount of
13 Sarbanes-Oxley or complete exemption, would you treat that investment differently?
14 As an investor looking at where to place funds, how would complying, not complying with,
15 affect that decision and the cost of the capital?

16 MR. RUSSO: Yeah, I think, first of all, they have a financial audit requirement that the
17 SEC mandates. They are being well-audited outside of the audit on control, and so, I am
18 comfortable with the success of compliance with that audit.

19 In terms of the compliance with the control audit, I think that most companies I talk to
20 sort of take the medicine in year one and they accept that, though it's expensive it may have
21 some ancillary benefit. Even this company found some. It's the years two and beyond, I think,
22 where the question really arises. And more importantly, it's really the question about lack of
23 clear guidance as to whether the Sarbanes-Oxley audit has the same tests as the financial audit

1 that the auditors, the public accountants are able to pull back a little bit from their absolute
2 standards that they seem to engage on the Sarbanes-Oxley side right now.

3 Those are two costs that I think are ill borne by this company. The first year's cost, I
4 suggest, are probably useful, though high. It's the multiple, subsequent years. And they would
5 have suggested that to the extent that there are only a few areas that are really the hot button
6 areas, whether it is income tax receivables or inventories, those areas that are really critical,
7 might be reaudited on rolling basis going forward.

8 It may even be that there is a holiday for three years once they pass the first audit, but
9 some way of relieving the company from doing this again and again and again would make a lot
10 of sense. Clearly, the value of relaxing this sort of rigid lack of flexibility the auditors feel they
11 have to comply with right now would be very useful.

12 MR. DENNIS: Sorry to keep hogging this, Herb, but so as an investor if you went to a
13 three-year or some other type of program, you would not increase the cost requirements or
14 increase your return requirements?

15 MR. RUSSO: Not a bit. Not a bit. After -- especially after going through the first
16 year, and we have already done it, so, no. I don't think we are going to catch great -- the great
17 mischief through this portion of required audit review. I think that certainly you have enormous
18 other areas that compliance is stiff and needs to be jet, but this isn't one.

19 MR. DAVERN: Herb, can I ask a question?

20 MR. WANDER: Oh, sure.

21 MR. DAVERN: Alex Davern on the 404 subcommittee of the overall committee. I
22 appreciate your coming to talk to us today. I have a couple of specific questions. One is, in the
23 U.K., you mentioned you invest in foreign companies as well --

1 MR. RUSSO: Yes.

2 MR. DAVERN: -- and obviously the U.K. and Canada and other countries have chosen
3 not to follow the 404 path, but they have called it a much more streamlined path, focused on the
4 tone at the top and things like independent audit committees and independent boards of directors
5 which give you perhaps more objectivity in terms of how you run a smaller business.

6 I am wondering if you -- it sounds like you don't discount U.K. Company, smaller
7 company, versus a U.S. smaller company because of a different regulatory environment. That's
8 my first question. And my second question is how you would view or how the company you
9 talked earlier on; their management might view the notion that for companies of a certain size we
10 would require only the management attestation, but perhaps eliminate the external auditor
11 attestation part of 404.

12 MR. RUSSO: To the second question, I think that the advice to the external auditor that
13 I think community seeks from the PCAOB would likely lead to a harmony so that both could
14 attest. And it's just absent that advice, absent the standards, that would allow the external
15 auditor, because they sign off on financial statements. It's just this quirky moment where there is
16 lack of clarity that leads to this extra expense and extra burden, and the unwillingness, for
17 example, for them to sign off at a level for which the management would be asked
18 to sign off in that case. I think you can drive them to the same outcome, but you just have to
19 have clear expression from both the SEC and the PCAOB that they have a shared standard.

20 MR. DAVERN: Are you aware by any chance of the incremental guidance that was
21 issued by the PCAOB and the SEC in May with the goal of achieving that purpose?

1 MR. RUSSO: I am, and the specific reference by the company I referred to, was that,
2 indeed, they know of it, but, indeed, no accounting firm is going to respect it because it hasn't
3 been in effect --

4 MR. DAVERN: -- so far it seems to say that it has been tried but it hasn't worked.

5 MR. RUSSO: Yes, but, clearly, as a goal that, I think, would alleviate an enormous
6 amount. And to the extent that that sort of release valve were allowed to be even more fully
7 expressed for smaller companies rather than the multi-national or the extraordinarily large macro
8 cap companies, I think that would be very helpful.

9 MR. WANDER: Let interrupt just for a second to indicate that Bob Robotti, a member
10 of the Advisory Committee has joined us. Hi, Bob.

11 MR. ROBOTTI: Hi. Sorry to be late.

12 MR. DAVERN: And on the first question relative to whether you discount U.S.
13 companies because of a different regulatory regime than the U.K. valuation method or do you
14 generally apply the same valuation method?

15 MR. RUSSO: No, I am not discounting them. I often invest in companies where their
16 families are still involved and control the businesses and they are public, but at the same time
17 have families that run and still influence the boards. So for me, it has to be a judgment about
18 the people with whom I am entering into business as an investor, so I have already crossed that
19 hurdle as to whether I can trust them at the start. And so the differences in the way that they are
20 measured based on U.S. versus foreign accounting standards, I don't stress that much.
21 And then, you know, the Sarbanes-Oxley requirement of independent audit committees, you
22 know, the advice towards an independent chair often has been already implemented in foreign
23 markets certainly.

1 MR. DAVERN: Certainly in the U.K.

2 MR. RUSSO: Yes, certainly in the U.K. and historically in foreign countries like
3 Switzerland is historically abiding by that. Anyways, so I think the judgment is already on
4 whether or not you are going to be treated fairly rather than how it is expressed by
5 the terms.

6 MR. DAVERN: Thank you very much.

7 MR. RUSSO: Okay.

8 MR. WANDER: Jim?

9 MR. THYEN: Yes. Tom, this is Jim Thyen. Could you articulate for us what you see
10 as the benefits of 404 or what shareholders see as the benefits?

11 MR. RUSSO: I think it is a second trip wire, so it should catch the miss. Auditing the
12 systems that track receivables and inventories, for example, ought to allow for discovery as to
13 abuse on valuing those items, for instance, that might only come up subsequently when it's
14 released that the financial statements have been misrepresented. That it's an early warning
15 system. If you have controls in place where you have a way to back-test the numbers before
16 time passes, it's an early warning system, I think, to make that sure that the controls
17 are right. A sort of notion of measuring twice and cutting once, so that you would have a chance
18 to at least see it beforehand. That's in the best case.

19 MR. THYEN: One of the items that an investor would dearly like to avoid, all CEOs
20 would like to avoid it, too, is restatement of earnings.

21 MR. RUSSO: Yes.

22 MR. THYEN: Do you see any connect point there or any value there in terms of
23 reducing the number of times that earnings have to be restated?

1 MR. RUSSO: I wouldn't find -- as I was -- as I understand the areas that come up
2 frequently, what has been discovered most often refer to areas of receivables and inventory and
3 income taxes. And I am not sure that those are really the areas that lead to the frequency of
4 restatements. That's my knowledge.

5 MR. THYEN: Okay, thank you.

6 MR. WANDER: Are there any other questions from members of the --

7 MR. GOELZER: Dan Goelzer. Can I ask a question?

8 MR. WANDER: Certainly.

9 MR. GOELZER: This kind of covers something that Alex touched on already, but I was
10 quite interested in your comment about the inability of the auditors to exercise judgment, and
11 that being the essential problem here. As Alex, I think, pointed out, the PCAOB issued a
12 statement in May of xx this year essentially stating that auditors are expected to exercise
13 judgment and to use that judgment to focus on the areas of real risk in control.
14 I take it from your comments that if we could make that real, if we could make that
15 philosophy actually permeate through the system, then many of the concerns that you have about
16 the cost benefit equation here would be alleviated. Is that a fair statement?

17 MR. RUSSO: Absolutely. That's the only thing that I hear back consistently, and it's the
18 plea for some relaxation of what would be perceived at the moment to be a zero percent sort of
19 materiality test. And it just seems like in this one area, separate from financial reporting, that
20 there is a requirement to go to the end of the earth to confirm the integrity of control systems.

21 As I said with the company, the seven or eight billion dollar market capitalization global
22 technology company, Palo Alto, at the end of auditing 400 -plus controls, they discovered a

1 \$10,000 misalignment. That doesn't mean that the process wasn't valuable; it just shows you
2 how fine the screen is, and so -- and I think it's the number one refrain that I hear.

3 Now it's clear that in the case that I spoke about earlier that the first-year costs were high
4 in part because accounting firm staffed their audit up with young, inexperienced newly hired
5 auditors. This year, after protest, they have a more seasoned and familiar team. So this year's
6 audit would go more smoothly and next year's would go more smoothly. It is just a question of
7 whether you are engaging in value-adding services in the first place. And I think year one, its
8 yes, especially if you can have some relaxation from an absolute test.

9 MR. GOELZER: Yes, the year one experience also would have been before the board
10 and the SEC issued these statements concerning judgment and focus on risk.

11 MR. RUSSO: Yes. I wonder whether it isn't in some ways, you know, this concept that
12 came up in the mutual fund of independent director proposals that went into effect sometime
13 back, I understand may have been reversed in a recent court judgment for being a solution that
14 was proposed without proper review of the cost benefit analysis. I am stepping on thin ice, but I
15 am sure it's something in this case again would be to try to understand it.

16 I don't know whether anybody has put forth data that suggests that in light of the controls
17 that we now have, we are seeing higher equity values. It's probably too soon to tell, but. I don't
18 know many investors who say because of Sarbanes-Oxley they can sleep more peacefully at
19 night from fear of fraud or mischief.

20 MR. BOCHNER: This is Steve Bochner. Herb, can I ask a follow-up question?

21 MR. WANDER: Certainly.

22 MR. BOCHNER: This is a follow-up question to Jim's of a few moments ago, and that's
23 your sense of whether for -- as you see restatements occurring out there, whether you think the

1 materiality concepts that exist today for SAB 99 are being interpreted correctly, are there too
2 many restatements, does it look like the standards work today? You mentioned that there is
3 some subjectivity in those standards, and I am interested in your impression as to whether we've
4 got the right test in place for auditors and issuers to figure out whether errors should give rise to
5 a restatement?

6 MR. RUSSO: And this is beyond -- this is on the financial statements rather than --

7 MR. BOCHNER: This is on the financial statements themselves, yes.

8 MR. RUSSO: I say that the problem with restatements, I think, on Wall Street and
9 among investors who are long-term minded is that it feels like a business whereby your focus on
10 meeting investor expectations that were, in fact, presented by management in many instances,
11 and then triggering compensation benefits that result from meeting those, those targets, to what
12 extent with frequency of restatements lowered later those compensation levels seemed to have
13 been forced and premature in some ways. I think that that's where, to me at least, the restatement
14 frequency, I would have trouble with it just because so much of compensation
15 is based on presented numbers, and once paid out, if those numbers are restated to show that, in
16 fact, sorry they really weren't the real numbers, it lends itself to mischief off that one important
17 guideline. So I am not sure how you end up tightening up the terms for that, but that's what I
18 would observe as an area of potential ongoing investor trouble.

19 MS. DOLAN: Herb, this is Janet. Can I ask a question?

20 MR. WANDER: Please, go right ahead.

21 MS. DOLAN: Hi, this is Janet Dolan. Thank you very much for your testimony. I am
22 the Chairperson of the 404 Subcommittee.

23 MR. RUSSO: Okay, nice to hear from you.

1 MS. DOLAN: You too. Thank you for your testimony. And you are reiterating a
2 number of points that I will say we have heard from a number of stakeholders in this matter.
3 And if I boil it all down, I think many people are saying: Can't we just find a way to
4 become more rational in the way we implement this requirement? And I think a couple of your
5 suggestions are ones that we are looking at. Could we spread the work out or could we get the
6 PCAOB or others to be much more clear about what the actual standard is because audit firms
7 are concerned about their regulatory legal exposure, so they need a very bright line.

8 MR. RUSSO: Absolutely. And the notion that a solution might be to let management
9 go forth and sign off on Sarbanes-Oxley audit results without the auditor signing off just shows
10 you how cart before horse that outcome is.

11 MS. DOLAN: We are trying to find a solution and so we welcome your input. I have a
12 question which is: If we aren't able to do either one of what you recommend, either spreading it
13 out or getting more of a bright line clarity around how to really implement this effectively, how
14 do you feel about the concept that shareholders should have the right to vote on this, that
15 shareholders should have the ability to have a say in whether this really is a good use of the
16 company's resources, especially as you get into companies, as it is in your case, end up costing a
17 more of a percentage and having a bigger impact on smaller companies than it is on larger
18 companies? As an investor, how would you feel about having the ability to weigh in on that
19 based on the company?

20 MR. RUSSO: I think it's in the realm of management discretion. For example, I don't
21 think we go into an environment where you have shareholders electing to apply either the '33 or
22 '34 Act on a company. It's the same substance, and I think what you need to do is simply
23 establish a recognition that your screen might be too tight in terms of what you are looking to

1 find, and then to relax that screen much as you do in financial accounting. Then I don't think
2 once you have relaxed it, then to go back in and let the shareholders decide whether they want to
3 tighten it up again makes that much sense, because, really, it's in the realm of the management
4 systems and the management efforts, I think, as I would see it.

5 MS. DOLAN: Thank you.

6 MR. RUSSO: Yes.

7 MR. WANDER: Are there any other questions of Tom? Comments? Bob?

8 MR. ROBOTTI: Tom, Bob Robotti.

9 MR. RUSSO: Yes, hi, Bob.

10 MR. ROBOTTI: Could you give us some idea -- one of the questions, of course, we are
11 looking at is the size of the company and the applicability and the cost benefit to be derived, and
12 obviously for much larger companies, the cost is less significant and, therefore, it is easier to
13 justify the benefit. How do you perceive that in terms of what is the range of companies you do
14 invest in and do you see in its application has more importance for small cap companies, less
15 importance, or is the cost benefit significantly different so there is a different standard to be
16 measured for smaller companies than larger companies?

17 MR. RUSSO: You know, it's a funny observation but I like the notion that the folks
18 with whom I spoke prior to coming here begrudge spending their money, as shareholders
19 themselves, unnecessarily. I mean, they would concede the first year even though it was a
20 million and a half dollars to confirm that everything was in working order, but seriously
21 begrudge the next three years of spending the same amount because it was in some ways their
22 money.

1 I think at the other extreme where you have a quite large public company with
2 decision-makers who may not be stakeholders whatsoever, you run the risk that the appearance
3 of Sarbanes-Oxley gives investors the false illusion that they are actually acting on their behalf.
4 And so, you have the two extremes. You have the small company where the owner and the large
5 shareholders say: I really regret having to write our money out in checks to do something that
6 really doesn't add incremental value over time. Where the opposite is the very large company
7 who says: I will write that check all day long because actually it is consistent with own benefit
8 to do it because it suggests that by doing so I am doing the right thing by my owners. And that,
9 in fact, may not be.

10 So I don't think -- to that extent, I think it is -- what I think is important is that they audit
11 the right thing and that once they have done it, they move on. And, clearly, you are right to say
12 that for large companies the marginal cost isn't nearly so burdensome. But it may suggest to the
13 investor something different than reality.

14 MR. WANDER: Okay. Do we have any other questions or comments?
15 Tom, we thank you very much, but we may come back to you and you may want to ask some
16 questions of your fellow panelists. Why don't we move on to Jane at the end of the table. And,
17 Jane, we would love to have you introduce yourself and then tell us your observations.

18 MS. ADAMS: Thank you. I actually do have some formal remarks prepared, if you
19 would accept them.

20 I am a managing director with Maverick Capital, Maverick's New York based hedge
21 fund. It's a long-short hedged equity fund managing approximately 25 billion in gross assets. A
22 portion of our assets are in a small cap fund. That we would define the criteria for that

1 differently than you. Maverick's investment style does require in-depth fundamental research,
2 and I think you will find our views a bit different from Mr. Russo's.

3 We, as investors, believe that we have benefited greatly from the requirements of
4 Sarbanes-Oxley and the requirements of the SEC. We have seen improvements in governance,
5 internal controls and greater transparency -- although, of course, more is needed -- through more
6 timely and detailed information that is being provided to investors. We believe that efficient
7 capital markets rely on investor confidence in those markets. If investors can rely on the
8 implementation of Sarbanes-Oxley by all, small and large companies alike should benefit from
9 the continued increased confidence of investors. Conversely, if Sarbanes-Oxley requirements
10 are differentially implemented, those registrants given exemptions should not benefit.

11 Full, fair and accurate disclosures are an essential component of efficient, liquid capital
12 markets. Internal controls are essential to assure accurate and reliable financial reporting.
13 Robust internal controls protect investors. Public companies have been required to have a
14 system of internal controls since 1977, I believe. As we can see from the many frauds
15 committed on the public, that requirement has not been observed, as many have likely cited to
16 you, particularly since we are the last group of panelists, bringing up the 1999 COSO report
17 analyzing fraudulent financial reporting between 1987 and 1997. That report found that
18 companies committing fraud generally were small.

19 Independent testing and assessment of internal controls is essential. Again, we have seen
20 that simply requiring companies to have in place an effective system of internal controls with the
21 expectation that auditors would test those controls has not produced compliance. External
22 testing of the existence and the effectiveness of the controls and reporting those results to

1 investors must be part of the framework to ensure that there is compliance. Nothing in Sarbanes-
2 Oxley says that a one size fits all solution is required for an internal control system.

3 All companies are competing for the same public investment capital. It's a privilege. It is
4 not a right to employ the public's capital and a key component of obtaining that capital is
5 obtaining the public's trust. Financial controls assure that shareholder -- assure shareholders that
6 their assets are being secured and that the information provided to shareholders is reliable. And
7 that's how trust is maintained. Therefore, there should be no class of public company that
8 receives an exemption from having adequate internal controls and reporting on their
9 effectiveness. They all compete for public investment dollars and have the same duties to
10 shareholders. If a company does not want to adhere to the rules for raising public funds, as we
11 have seen in the Daily News, articles suggest that there is plenty of the venture capital and
12 private equity funds looking for opportunities.

13 Investors do have a different appetite for risk, but that risk shouldn't be satisfied
14 because of inadequate financial information or because inadequate controls may impair the
15 reliability of the information that is being provided. Establishing a two-tier population of
16 companies, one which has independently reviewed, tested and effective system of internal
17 controls and one that doesn't, necessarily will add a risk premium to the class of companies that
18 do not. One would expect that second group to experience higher costs of capital and decreased
19 liquidity if the protections provided to investors for each investable dollar differ due to size.

20 If different standards are permitted, whether GAAP or internal controls, any financial
21 statements and filings prepared under this light version should have large red warning labels
22 alerting investors to that fact. These warning labels are particularly important if we want to

1 avoid unfairly penalizing companies that have established an effective system of internal control
2 and compliance with GAAP.

3 As to the cost of compliance, in our view, the cost of compliance with Sarbanes-Oxley
4 has not influenced management's investment decision. We have viewed these costs from a
5 qualitative perspective as corporate investments, much as some justify the costs of R&D or
6 marketing. When companies have indicated that their costs have and will be significant due to
7 extensive remedial efforts necessary to come into compliance, we view this as a needed catch-up
8 of previous under-investment. Moreover, in some cases it has been clearly demonstrated that
9 management did not have a grasp on its business.

10 I've also taken the opportunity to address a couple of your questions specifically.
11 Question 4 focuses on the effects of the U.S. regulatory environment on the U.S. markets. U.S.
12 capital markets are the deepest and most liquid and continue to provide investors with greater
13 protections than any other markets in the world. These protections include conformity with
14 GAAP and test standards, oversight and regulation. This comprehensive combination of
15 standards, controls and oversight does exist as investor protection for investments in foreign
16 companies whose securities are not regulated in the United States or registered.

17 Question 6 asks about the potential diversion of management focus away from
18 operations. Sarbanes-Oxley is critically entwined with capturing, measuring and reporting the
19 financial consequences of operations. If managements have not been paying attention to this
20 information, they should have been. As I mentioned, certain past failures have highlighted the
21 fact that managements have not had a grasp of their business.

22 Question 13 raises concern that small private companies may be deterred from going
23 public. I believe that this question is better reframed: Should companies with ineffective

1 controls and the added risk of producing misleading, inaccurate, incomplete and unreliable
2 financial statements be permitted to cloak themselves in the guise of compliant companies and
3 take money from investors, at least in the public?

4 Question 14 is disturbing as it raises the question that some companies, based on size,
5 should be permitted to access the public markets without complying with certain investor
6 protection measures. This question should also ask how the cost to investors should be measured
7 against the billions of dollars of investment losses suffered, against the impact on markets when
8 their looper is perceived to be damaged goods. What should happen when entire sectors get
9 penalized for the failure of some? Innocent control complaint companies get tarred with the
10 same broad brush inhibiting their ability to raise capital in the markets as efficiently as they
11 could.

12 Final comment on the big GAAP/little GAAP, GAAP or GAAP Light, however you refer
13 to it, landscape, is one that actually I find quite disturbing and is disturbing for investors. GAAP
14 should be neutral. GAAP should be applied comparably by all companies. Light transactions
15 should appear similar. Unlike transactions should appear dissimilar. Companies by virtue of
16 size should not be able to choose among multi GAAPs to structure transactions and keep relevant
17 information from investors. That does end my prepared remarks. Thank you very much.

18 MR. WANDER: I would like to just mention one thing. A lot of people have
19 commented on the COSO study that I guess covers eleven years. And I think if you read the
20 study, which I have now done three times, you will find (A) they commented they were surprised
21 that there were very few fraudulent cases reported by the SEC. And, secondly, if you look at the
22 array of companies, it really comes down to what their percentage of the landscape was. In other
23 words, 27 percent of the companies were New York Stock Exchange. Well, that's the universe.

1 And so, the smaller companies, while there were more of them, the fact is there are more
2 smaller companies and they are not a greater percentage of those companies in the other
3 categories. So I think that study deserves a little more attention than just saying there were a lot
4 of small companies who had SEC problems with their financial statements. Why don't we open
5 it up to questions. Jim?

6 MR. THYEN: Yes, Herb. Hi, Jane. Thank you for providing your insight to this group.
7 Given your position and your feelings on the importance of Sarbanes-Oxley and the privilege
8 of being a public company, what is your view now that we are where we are? The law is
9 enacted, the process has started, should smaller, or should companies that were in the public
10 market before the rules changed, should they have a choice of leaving the market? Should the
11 requirements for exiting the public capital market in the United States be re-examined?

12 MS. ADAMS: I don't know that I can adequately answer that. I do understand that there
13 are difficulties in exiting markets or there are complexities in doing so. Certainly, if companies
14 are interested in exiting the market because they do not choose to provide full and fair
15 disclosures to investors, I think investors are likely better off having them exit the market.

16 MR. THYEN: Thank you.

17 MR. WANDER: Leroy?

18 MR. DENNIS: Thank you, Jane. Leroy Dennis. I really have two questions but I will
19 start with the first one. You mentioned that there were billions of dollars lost in the markets, and
20 we all saw that in our own portfolios, and that a few companies can taint a sector. I am
21 wondering if you think of those -- I guess I would challenge whether any of those are what we
22 define as micro cap companies where they would actually taint a sector, and I
23 would argue that they probably didn't cause any of the losses in the markets. But the question I

1 have for you is: Should there be a difference? Right now the fact of the matter is that
2 smaller or micro cap public companies, they probably don't have a very good market float. They
3 really don't get all of the advantages of a public company with stock trades and any kind of
4 volume, so they have liquidity.

5 So should there be a difference for companies who maybe don't, although they are public
6 and they report public, but they really don't have those same accesses that a WKSI company or a
7 much larger company even in our smaller definition has in access to capital?

8 MS. ADAMS: We do not invest in micro-cap. I don't think it would appropriate
9 necessarily for me to comment on that. We do invest in populations of companies that would fall
10 into your small definition versus micro-cap. We are very clear that we believe that as
11 the toll for accessing public capital there are requirements and those requirements should include
12 the full compliance with the aspects of Sarbanes-Oxley, including Sarbanes-Oxley on an
13 annual basis, audited by independent auditors and reported to shareholders.

14 MR. DENNIS: Thank you. My second question was: As you think about 404, and you
15 mentioned one of the aspects of it, I believe, was to help prevent fraud. Are there
16 aspects of 404 that maybe don't accomplish that objective? Especially as I look at smaller public
17 companies, it seems to me that CEO, CFO type occurrences are really the ones that we have to
18 be concerned about and less concerned about transactional testing. But I would be interested in
19 your views on that.

20 MS. ADAMS: We received a set of follow-on questions in terms of testing tone at the
21 top, and it was quite a surprising question to us, that controls, while certainly tone at the top can
22 give you a sense of the environment for which -- in which the internal control process is taking
23 place, that as investors, we want to understand that what is being reported and the manner in

1 which it is being reported, that the line items that are being represented as cost of sales versus
2 R&D versus SG&A are actually the ones that are comparable to what their peers are reporting.
3 And I think it requires an internal control system to be able to develop that information.

4 MR. DENNIS: Okay, thank you.

5 MR. WANDER: Other comments, questions?

6 MR. DAVERN: Her, Alex here. Jane, thank you for your testimony. A
7 couple of questions. When you mentioned that you apply a different criteria to define smaller
8 public or small cap companies, I am just curious as to what criteria you use?

9 MS. ADAMS: We base it on liquidity, the volume.

10 MR. DAVERN: What sort of numerical numbers, what sort of market cap numbers? Is
11 market cap a factor?

12 MS. ADAMS: Certainly, we are aware of market cap, but, really, we would be looking
13 at the volume of trading on an average daily basis. And so the companies that end up being
14 qualified based on that criterion would generally be between 300 million and a 2 billion market
15 cap.

16 MR. DAVERN: Okay, that seems consistent with what have we heard from others. I
17 appreciate that. My other I guess question to you -- two questions. One is: Is it your perception
18 that as currently being implemented will be effective at significantly reducing financial fraud by
19 senior executives is one question. Then the second question is: What percentage of revenue in
20 general, I mean if we were trying to scale 404 and focus it on real valuable stuff, where -- as an
21 investor, if you look at cost of implementation as a percentage of revenue, at what point does it
22 start to become questionable as to whether it is excessive that the company should

1 consider in your view exiting the public markets for a private market because of the cost relative
2 to their size, or have you given that any thought?

3 MS. ADAMS: Well, second question first, did give that thought. Again, it was some
4 follow-on questions that we received and discussed internally. And this, too, had us kind of
5 scratching our heads because the logic was that if this was going to be such a significant cost for
6 companies, that then we interpreted if their control systems were so slovenly that it was going to
7 be a significant dollar cost, then why is giving them a break better?

8 MR. DAVERN: Perhaps I could engage you a little bit on that. As a public company
9 myself at National Instruments, which would fit in your purview around \$2 billion, I think we
10 have excellent financial controls, and, yet, the process as implemented costs us almost \$4 million
11 last year. Just to get you into a conversation, you know, when the SEC originally implemented a
12 rule on this, the intent was that it would cost \$90 thousand per company. And I think the reason
13 that we are all here today is that the intent of how 404 was meant to work, it turned out costing
14 about times more than was intended, and it's that gap between the intent and the reality that has
15 drawn us all together to try to find a better way to implement the spirit of 404 without basically
16 wasting money if we can. And so --

17 MS. ADAMS: Could I just get a sense of when you say it cost \$4 million, and if this
18 was an element of the question also in terms of 404 compliance?

19 MR. DAVERN: Sure.

20 MS. ADAMS: \$4 million, that was solely involved in management's --

21 MR. DAVERN: It is the external audit fee and a commitment of about 25,000 internal
22 hours that document that we have no significant deficiencies and no material weaknesses.

1 MS. ADAMS: And, again, given that auditors have been required if they have been
2 relying on the internal control systems to have tested them all along, what did that tell you?

3 MR. DAVERN: Well, the reality is auditors were not required to test internal control
4 systems all along. It was not a requirement of a financial statement audit.

5 MS. ADAMS: If they rely on them.

6 MR. DAVERN: Yes, but most auditors will do a substantive audit of your balance sheet
7 at the end of the year and they won't test all the detail transactions that happened during the
8 course of the year. As it is being interpreted, it created a major new requirement on external
9 auditors.

10 MS. ADAMS: But isn't your point, then, that there hasn't been the flexibility in
11 application --

12 MR. DAVERN: Yeah, if this had cost \$90,000 I wouldn't be on this committee and I
13 wouldn't be paying attention to this subject. The reality is what was intended to happen and what
14 actually happened are orders of magnitude different, and we are trying to figure out
15 how to bring it back to the original intent. At least that's my purpose in asking the question.

16 MS. ADAMS: And, again, I do find it concerning that there would be a different strata
17 developed for companies who just simply wouldn't have to comply with it at all.

18 MR. DAVERN: And certainly I appreciate your view on that completely. One of our
19 theories, at least one of my thoughts is, from all the investors we have talked to before, people
20 who have testified, is that there already appears to be a different strata in terms of criterion
21 applied by investors in evaluating risk of different companies based on size. As you have just
22 laid out, you have a number of criteria that you apply that assign a base that lead you to make
23 certain risk decisions based on investment. I am not certain that's the answer, but I just wanted

1 to get a sense if you had any concerns with the reality that it appears that it costs
2 almost every single company an order of magnitude more than was intended, and do you feel
3 that there is a need to rectify that or are you comfortable with the current scenario?

4 MS. ADAMS: I do not believe that in any business aspect it's appropriate to spend
5 money injudiciously. If there is an ability to streamline the -- from the perspective of the
6 auditors, of course, we would be supportive of that. I cannot comment on how the auditors have
7 viewed the implementation of Sarbanes-Oxley . I know there has been frustration on the parts of
8 auditors that the guidance wasn't forthcoming and then after the fact they heard that they had
9 gone over the top and should have perhaps curtailed some aspects of their procedures. With luck
10 and effort, I am sure that will be clarified as we go forward. I think that would be great.

11 MR. DAVERN: Any thoughts on, is it your perception, do you think that investors in
12 general perceive that 404 will be effective at preventing the kind of financial frauds that we saw
13 in Enron, et cetera?

14 MS. ADAMS: I think that investors are looking at various elements of Sarbanes-Oxley
15 as providing them with information that would give you a hint that there was some manipulation
16 of information that shareholders were receiving or weren't receiving at all prior to Sarbanes-
17 Oxley. And in terms of financial fraud, I think that, speaking for Maverick's investment team,
18 that we will be quite wary of companies where there are material weaknesses identified and
19 where management has not done a good job of identifying for us what the nature of those
20 problems were and what remedial efforts have been undertaken to correct that.

21 MR. DAVERN: And one last follow-on question, Jane, and that's in relation to the other
22 aspects of Sarbanes-Oxley, the whistle blower provision, independent audit committees, majority
23 independent board of directors, et cetera. Do you have a view on the effectiveness of those

1 elements of the law in terms of improving governance and perhaps help reducing fraud vis-à-vis
2 404? Do you think they are as important, more important, less important, or I am not sure if you
3 thought about this or not?

4 MS. ADAMS: I do have, what a surprise, some views on that, too. And we do believe
5 that having a strong independent board is very important. I don't think that I can put them on
6 scale, though, with 404 on one side and some of the other elements that -- in terms of the
7 characteristics of the board and the audit committee and tell you how that balances out.
8 We do evaluate the board, particularly how likely is this board to be representing ours, as
9 investor's, interests, versus interests of other parties, but most particularly management.

10 MR. DAVERN: Thank you very much, Jane. It has been very useful.

11 MR. WANDER: Kurt?

12 MR. SCHACHT: Jane, thank you for being here. Kurt Schacht from CFA Institute.
13 Just to sort of follow on some of Alex's thoughts, I think everybody -- not everybody but
14 many of the people that have been involved in this debate acknowledge the fact that Sarbanes-
15 Oxley was implemented in some haste, that it was implemented in a crisis situation, and that
16 there are probably things -- even the authors of the bills have suggested that there are things that
17 need to be looked at and possibly tweaked. So I think there is a suggestion that there are things
18 that could possibly change with this bill, with this and in the approach to internal control audits.

19 Is there anything else that you or your firm has discussed that you would think might
20 reduce costs? For example, would you be comfortable with knowing that, in fact, there internal
21 controls at all levels of companies big to small, that there is some degree of independent review
22 of those controls whether it rises to the level of a full audit in all cases, but maybe to some lesser
23 standard of review for smaller issuers? Would that have any appeal to you or your firm?

1 MS. ADAMS: Kurt, I believe that the objective of internal controls is to insure that if
2 there is a material misstatement potential, it will be identified and that will be done on a timely
3 basis. Companies have been required to have an internal control system in place for decades;
4 yet, we know that, based on the frauds that have occurred in all sizes of companies, that -- that
5 simply the requirement that they exist has not been sufficient to have them exist in an effective
6 manner.

7 And, you know, I don't know how to respond to your question when it starts out being
8 framed as a document written in haste, where even the authors perhaps would rewrite parts of it,
9 because the 404 section is quite short, a couple of paragraphs. And I am not sure that there is
10 much that could be rewritten there, as opposed to, yes, putting the effort into having
11 implementation guidance that perhaps pulls back from the excessive auditing or the areas of
12 excess where -- that we have been hearing about in year one.

13 MR. WANDER: Could I follow-up on that? I think this is somewhat like Alex's
14 question, and I will start with your citation to the COSO fraud study. One of the things that the
15 fraud study indicated for the companies that actually experienced SEC sanctions for having
16 fraudulent financial statements was the fact that they essentially didn't have independent boards,
17 a great number of them. Surprisingly 70-some percent involved CEOs. The audit committee
18 was either non-existent or certainly not independent. There obviously wasn't a whistle blower
19 statute at that time.

20 So I think in trying to interpret Kurt and Alex's question, how much added protection or
21 comfort does that -- do those things add to the mix that might permit us to sort of figure out to
22 adjust 404 to take into consideration those items that didn't exist five years ago that do exist
23 now?

1 MS. ADAMS: The items that you mention, so, for example, a strong independent board
2 and independent audit committee with financial expertise, I still do not think that that is at a
3 level that insures that transactions, as they are accumulated through the reporting process, are
4 consolidated and reported in a manner that can assure that the line items, whether it's the income
5 statement, the balance sheet or the cash flow statement or the disclosures in the notes are going
6 to be adequate. I am not sure that is satisfying you --

7 MR. WANDER: No, no, no. We just want your views.

8 MR. DENNIS: I think if maybe I can ask a follow-on that maybe will clear this up.
9 I am hearing you say that audit committee, whistle blower, those kind of things are
10 effective at detecting fraud, more effective at detecting fraud, but the ancillary benefit of to
11 you is that casual mistakes in a financial statement are more likely to be caught by the controls
12 that are in place and tested by 404? Is that -- that's kind of what I have been hearing, because
13 that's getting into are individual transactions revenue recorded correctly, maybe not testing or
14 maybe not as effective at whether or not the CEO and the CFO got together and decided to pony
15 up a transaction. Am I getting what you are saying there?

16 MS. ADAMS: We continue to see efforts -- let me -- there are various elements of
17 controls that were required, mandated by Sarbanes-Oxley. We support them. We believe that
18 they will result in better investor protections on many levels. That a strong board would
19 challenge a management that continues to make decisions that are off the fairway
20 as opposed to in terms of reporting are at the extreme, as opposed to reporting in a manner that
21 clearly and on a balanced basis provides comprehensive disclosure as to opposed disclosure
22 that's meant to mislead or hide.

1 Yet, there can be equally an exposure to restatement and loss for companies that simply
2 didn't know that that accounting standard existed, or as we saw with leases, that it existed for 20
3 years and, yes, they are expected to comply with it. I heard some of the questions that you were
4 focusing, that you were addressing to Tom in terms of the benefits of restatements or whether
5 these were harming shareholders. And, in fact, I think that it's very important that restatements
6 are judiciously used in order to ensure that the playing field remains the one that the standard
7 setters and the regulators have agreed is what defines the playing field.

8 If someone is off the playing field and isn't being called out of bounds, it harms those
9 who stay within bounds. And I think it's important to investors to have that sense of confidence
10 that the calls are going to be made and the consequences will be reflecting the financial
11 information in the way that standard setters and regulators have expressed as their views that it
12 should be represented.

13 MR. DENNIS: Maybe a little different question. You mentioned restatements and
14 we've obviously seen a large increase in the number of restatements in the past few years.
15 Do you sense that that is just people being less tolerant? Is there just more being identified? Do
16 we need additional guidance in what materiality is? Should there be a more of an
17 objective standard on materiality as opposed to a subjective standard? I would like your views
18 on that.

19 MS. ADAMS: I think I do not have the evidence to support this, and one reason for
20 citing COSO is because it was a relatively recent study, I am not aware of others who have gone
21 into the AAERs and aggregated the data in a way that would be useful or helpful in formulating
22 the responses.

1 I do believe that there is additional guidance that's necessary for materiality. I,
2 likely, would have views that differ from the majority of preparers on the direction that that
3 guidance should take. I believe, and anecdotally I would suggest, that one reason for the
4 restatements is that finally people were taking a look at the consequences of the systems they had
5 in place and they were finding that they were not complying with existing requirements. In fact,
6 some of the restatements we would say have confirmed aspects of investment VCs within our
7 investment team, so...

8 MR. DENNIS: I take it from your comment that you would want a tighter standard on
9 materiality than what preparers would want?

10 MS. ADAMS: Yes, full and fair disclosure. I was at the SEC when it wrote the SAB 99
11 on materiality. I think we could have gone a lot further. I think that that did a good job in saying
12 there is no rule of thumb, don't rely on the rule of thumb, that there is contextual information
13 that makes one penny critically important, and that all information have to be assessed, has to be
14 assessed in determining materiality. I understand that the SEC is going to be producing this fall
15 some guidance on materiality. I don't know quite the nature that that will take.

16 MR. DENNIS: I don't disagree with your comments. I guess the only comment I would
17 make is that -- excuse me -- that obviously the tighter the standards are, the more costly they are
18 and probably the more restatements we are going to get, which is going to -- so there are some
19 ancillary effects of those kind of things. But I agree with what you are saying.

20 MS. ADAMS: But restatements are not bad if it is necessary to reflect the information in
21 a manner that makes that company comparable to what its peers are doing. I mean, there is
22 relevant information presumably there. And an assessment of materiality is based on how
23 relevant, how useful, would this make a difference in user decisions.

1 MR. DENNIS: Thank you.

2 MR. BOCHNER: Herb, it is Steve. I've got a question if I have time?

3 MR. WANDER: Go right ahead.

4 MR. BOCHNER: It's Steve Bochner, Jane. Thanks a lot for coming here today and
5 talking to us. I think your views are important to hear. As I listen to you and listen to some of
6 the questions of the committee, I can't help but think that there are sort of two different levels of
7 dialogue going on. And one is the idea: Are controls important? Are accurate financial
8 statements important? And I think you get violent agreement among all the committee members
9 that those things are important and I think that's one of the themes that you have been expressing.

10 I think another level is calibration, and I want to make sure we've really heard your views
11 on that, because you could imagine us saying well maybe more needs to be done. In other
12 words, where we landed with respect to governance reform, where is, where the independence
13 rules are, we could --this committee could come out recommending even more, you know, more
14 internal audits, more frequent internal audits, more cost, more expense. So we are really -- I
15 think this committee has not been formed for the purpose of questioning whether internal
16 controls are good, or materiality, or whether accurate financials are important. I think we all
17 understand and can agree with you on that. I think it's really the next level question. It's
18 calibration. And maybe what you are saying is, no, we've got it right, we've got it perfectly right
19 where we are on this sliding scale, this scale of how much regulatory burden should we impose
20 on companies to achieve accurate financials. We got it exactly right. And that's what I hear you
21 saying.

22 And I think it would be good if you could just affirm that, because I think what we are
23 doing is saying now that we've agreed that internal controls are important, all of the things that

1 we have, we, Congress, NASDAQ, the NYSE, the SEC, have adopted this huge set of rules.
2 Now that we have them in place and we can step back and look at them on a calibration scale, we
3 got it exactly right. And that's what -- I think that's what this committee is trying to do is the
4 calibration issue as opposed to the higher level question of whether internal controls are
5 important. And I think we already bought off on that and I think we understand that.

6 So I guess I am just trying to confirm that you are basically saying nice try, guys, but on
7 the sliding scale of regulation versus cost, the rules in effect today got it exactly right, because
8 that's really our job on this committee.

9 MS. ADAMS: The requirement for management to review and assess the effectiveness,
10 and for the auditors to conclude on the effectiveness and report that to shareholders has
11 been beneficial to investors. It's been beneficial to Maverick.

12 I cannot -- I do not feel that I can comment on whether it required all that the audit firms
13 did in order to achieve this benefit. Clearly, there is -- there is considerable benefit that we have
14 received. It took great amounts of effort to surface some of the areas where there have been
15 significant deficiencies or material weaknesses. We are glad that those resurfaced. I don't -- I
16 am not able to comment on whether less of an effort would have surfaced those.

17 MR. WANDER: Are there any other comments, questions? I would like to ask one. I
18 think during your prepared remarks you indicated that without this, if smaller companies were
19 relieved, I guess, from the burden, that they would experience higher capital costs. We've
20 actually had conflicting views on that, the fact that if you don't spend the three cents or seven
21 cents, you would have a higher market value. And we've had some instances where companies
22 have, in effect, de-listed but provided people with information and their stock price has gone up
23 and they attribute it to that. But nothing other than episodic sort of stories on that. And we

1 haven't found any literature and I wonder if you have any support in terms of studies or anything
2 on that issue?

3 MS. ADAMS: No, I don't have anything that is footnoting those remarks. But it would
4 certainly influence the amount, the allocation of our capital.

5 MR. WANDER: Okay. Any other comments?

6 MR. CLOUTIER: Herb, Rusty Cloutier. If I could, I would like to follow up on a
7 question that was asked earlier and kind of follow through about the quickness of Sarbanes-
8 Oxley. It did pass in three weeks, and one of the things, I think, if they went back and looked at
9 it now is that they would very much look at the involvement of some of the large financial
10 investment firms that had paid over \$7 billion in penalties to their investors for misleading
11 information. And one of my questions would be: Does Maverick look at the investment advice
12 being given?

13 I know that's another big worry out there still with hedge funds and everything else, and
14 people sitting in board rooms and these investment bankers show up with these great ideas, and
15 the accounting firms like Arthur Andersen say, "Yes, we have looked at this and this is okay."
16 You know, there are still a lot of stories floating around, IRS and other things. I think that's one
17 point that has really not been corrected and I was wondering if Maverick has looked at any of
18 that. From my understanding of Enron and WorldCom and the amount of money that Chase and
19 Citibank have paid out, showed that they kind of led them down a path that maybe would have
20 been interesting if they didn't lead them down that path.

21 MS. ADAMS: Maverick has great confidence in the expertise and intelligence of its
22 own investment team. I don't think that I can go much further than that in terms of really
23 answering the question you are asking.

1 MR. WANDER: Okay.

2 MS. DOLAN: Herb, I have a question.

3 MR. WANDER: Sure, Janet.

4 MS. DOLAN: Jane, thank you very much for giving us your thoughtful answers and
5 taking all the time to help us work our way through the challenges that we have. I would like to
6 follow-up on both Steve and Herb's line of questioning, which is, as you can tell just even from
7 the two investors who have spoken here today and then all that we have heard from, investors are
8 not of like mind and are not speaking with one voice on how important this is to them. Some
9 feel that the calibration is way off, and others, like yourself, seem to feel that the calibration is
10 much closer to where you want it.

11 So my question is, but what everybody, I think, seems to want is transparency and
12 disclosure so that you can make your investment choices, so if we were to exempt a group of
13 companies or have companies -- smaller companies required to comply with standards less than
14 the full auditor attestation, but the market knows that, investors like yourself can either choose to
15 invest in them or not or raise your expected return on your capital requirement to do it. And
16 those companies if they find they have trouble getting capital can then voluntary choose to take
17 on greater disclosure and choose to voluntary have audit attestation. How would you respond to
18 that, that the real important thing is let the market decide, disclose and provide transparency and
19 then let the free market operate as they should and investors can determine for themselves which
20 companies they want to invest in and how important they feel the audit attestation is to those
21 companies?

22 MS. ADAMS: I am a firm believer, just to be repetitive, that if a company wishes to
23 access public capital, that it should comply with all the regulatory requirements, and that if it

1 doesn't, it can stay as a private company and find its capital from its management, from VCs or
2 private equity.

3 Certainly if there were to be two tiers of companies complying with different sets of rules
4 each of them vying for the same public capital, transparency and warning labels would be
5 essential so that investors were, on the face, notified that this information did not come with the
6 full package of protections and controls. Or if you were talking about different GAAP, which I
7 would find that also, that investors weren't misled and didn't have to read through to the notes to
8 realize that this company was effectively on a cash basis and there were significant accruals and
9 obligations not being recorded.

10 MS. DOLAN: I just have a factual point I want to follow up with because I might have
11 missed it in your statement. I take it that your firm invests in no companies outside of the United
12 States?

13 MS. ADAMS: We do.

14 MS. DOLAN: And --

15 MS. ADAMS: We have capital allocations internationally, I believe, on every -- in
16 every sphere.

17 MS. DOLAN: And you expect and want, then, to hold U.S. companies to a different
18 standard than those?

19 MS. ADAMS: We find that the information that we can get in terms of the financial
20 information internationally is significantly less robust in all aspects than what we have available
21 to us in the U.S. It does not mean that we are not allocating dollars there, but that are our
22 investment process takes on different characteristics for those companies versus those in
23 the U.S. It is not a question of one dollar competing in the U.S. or internationally and making

1 a choice on the information, the relative information. It's a decision that we would want
2 exposure with different international elements to it.

3 MS. DOLAN: And have your investments outside North America grown significantly in
4 the last five years?

5 MS. ADAMS: I would rather answer that that Maverick has done fairly well in the last
6 five years.

7 MR. DENNIS: This is Leroy, if I can ask: Do you require a different level of return for
8 companies, then, that are not subject to U.S. regulation before you will commit those dollars?

9 MS. ADAMS: We require an awareness of the risks involved in getting that return, and
10 so we are balanced there.

11 MR. DENNIS: I'm sorry, I am not sure I understand what that means, but -- so you
12 know the risk going in that there may not be controls operating effectively if you invest in a
13 French company, so to speak, and I assume that has effect on what you either decide how much
14 to commit or what you want as a return?

15 MS. ADAMS: For example, a French financial institution that might not even be
16 required to record loan losses, I mean, certainly that influences -- I do not believe that I can
17 answer your question --

18 MR. DENNIS: Okay.

19 MS. ADAMS: -- because it's a relative decision, and we are -- we do evaluate where we
20 would want those international dollars placed and the relative risks in terms of which sector
21 would receive those. I can't be more specific to your question of whether a 20 percent return in
22 the U.S. versus a 22 percent return is an adequate compensation for the significantly less robust
23 financial information that we have. It is not timely. There is not one set of GAAP.

1 MR. DENNIS: But I guess, then, from that example I would surmise that there would be
2 capital available to companies that, as Janet said, maybe provided a lesser degree of compliance
3 with the standards. It certainly may cost more but it would be one more risk with the fact that
4 there is less liquidity in the financial statements, less trading in the securities, smaller, more
5 concentrated, all those risks you are going to take into account and one additional risk you might
6 take in -- or investors might take into account might be different levels of controls if that was
7 what was ultimately recommended and adopted, but there would still would be capital available,
8 you would just have to deal with what it would cost you.

9 MS. ADAMS: Hypothetically.

10 MR. DENNIS: That's all we have. We have no fact right now anyway, so I think that is
11 all we are dealing in.

12 MS. ADAMS: But, I mean, in the United States, typically we wouldn't evaluate the risk
13 element of our exposure based on the fact of how unreliable is it, is this information that will be
14 provided.

15 MR. WANDER: We should move on. Jane, thank you so much. And I wanted to point
16 out, unfortunately, I didn't want to interrupt, but your former colleague, Commissioner
17 Goldschmidt was listening to you, but he just had to walk out.

18 MS. ADAMS: I hope he wasn't shaking his head.

19 MR. WANDER: No, no, he wasn't shaking his head. And I'm sorry he left, but I just
20 didn't want to interrupt the flow of the questions to say hello to him, which I was going to do as
21 soon as I had an opportunity. Tom, you have been very patient, and we appreciate your coming
22 down. I would like to call Tom Duncan from Frontier Capital Management now.

1 MR. DUNCAN: My name is Tom Duncan, I am President of Frontier Capital
2 Management, a Boston-based institutional investor. Our clients are largely corporate pension
3 funds, foundations and endowments. Our focus is heavily on the small and mid cap sector of the
4 market. We manage about something over \$5 billion, and about half of those assets are small
5 cap, as we, like Jane, defined it within the range of the Russell 2000, so 200 million to 2 billion.
6 We really do not invest in micro cap companies.

7 For me, I was sort of a late entry into this panel and my opinions are not as well written
8 as Jane's or Tom's, but I think in looking at this in the last few days, we would agree that the
9 goals of 404 are laudable. It's important after all the problems of the last few years to reassure
10 the public trust and investors' trust. What I hear is an issue of implementation, whether the goal
11 is to avoid fraud or to have, through this process, businesses run better. I think the goal is largely
12 to avoid fraud.

13 And if that's the case, it may be some regulatory overkill relative to smaller cap
14 companies. And there has been a lot of discussion or several times mentioned what the costs of
15 these regulations are relative to these companies' revenues. I just did a little simple math to I
16 think highlight that maybe if you look at it relative to their profits, it would be a more
17 appropriate standard. So a small cap company, it seems like there is some consensus that the
18 incremental cost for a hundred million dollar revenue company might be a million dollars. We
19 have done some surveys in the last of couple of days at our firm and that seems to be about the
20 expense. And just say arbitrarily that those companies are doing percent in terms of pre-tax
21 margins, that is percent of their profits is going to conform to these new regulations. This is a
22 very substantial cost relative to a \$5 billion company that some studies have shown might be

1 spending \$10 million, or ten times as much, but it is only two percent of their cost. It seems we
2 have to be cognizant at some point of the cost.

3 Now, there was a comment made about 404 light. I don't think any of us are advocating
4 that we don't have strict standards for companies of all sizes, but I think that if the regulations
5 could be streamlined to some extent, and I can't give you chapter and verse as to how you would
6 do that, but some it would just be some sensitivity to what the processes are in a smaller
7 company relative to a large multi-national multi-line company.

8 One of our analysts did a survey of 20 companies that he followed in the last week for us,
9 and I know that we are not responding to the needs of companies at this point, but at least we
10 could be sensitive to them. And of those 20 companies only one said I believe that 404 was
11 worth the incremental costs associated with its implementation. It seems to me just listening to
12 the debates today that if we said, okay, there is a cost, and it could be substantial and maybe it
13 will be 10 percent of profits in year one to get all of these ducks in a row and to get all of the
14 processes in place, that people would accept that. There could be full disclosure of what those
15 parts were, understood that everybody would be standing on a level playing field, and then have
16 some audit to just conform that, in fact, the processes are still in place. But what I am reading is
17 that these second, third year costs are not declining very much. And while not wanting to put an
18 overly cynical hat on, we have a declining number of public accounting firms, four majors who
19 audit 97 percent of the companies in the United -- public companies in the United States. And
20 for them, it's something of an annuity, and there is very little incentive on their part to streamline
21 this process.

22 And I think companies call out to regulatory authorities and the legislature to come up
23 with some mechanism where there is some countervailing balance against the normal profit

1 seeking incentives that are associated with these regulations for the public accounting firms.
2 And I will stop there and ask for any questions.

3 MR. WANDER: Sure. Thanks, Tom. Questions? Jim?

4 MR. THYEN: Tom, this is Jim Thyen. Would you share with us your view,
5 speaking of this area of cost, how that relates to the different markets, the different sectors in
6 which companies compete? I guess, do you agree that -- is it a correct view that different
7 markets have different margins?

8 MR. DUNCAN: Absolutely.

9 MR. THYEN: Different room for various cost structures, make-ups of cost? How do
10 you see that relating to the extra -- the regulatory burden?

11 MR. DUNCAN: My sense is, and I haven't dug as deeply into this as others on this
12 panel probably have, that there is this sort of one size fits all and we are going to have these same
13 processes whether they are entirely relevant to the keys for a company, an energy company is
14 going to have different issues that are material to that company than a retailer is, and the margins
15 in the business are going to be different, and the costs.

16 So having these rigid standards that have to be applied across industries, doesn't seem to
17 be -- I think the issue of materiality and accounting firms, the management making some
18 judgments that should be fully disclosed and understood by investors as to how -- what they are
19 measuring and how they are measuring it are critical. But I don't think we can have a pure
20 cookbook that spreads across all industries.

21 One of our analysts was talking to a company just yesterday and they were an energy
22 company. And, clearly, today when energy is scarce, people want to use all the resources they
23 can to go out and find new oil and gas, which is what this company is doing. Well they had to

1 defer a very significant percentage of their cash flow into these meeting new requirements, and
2 turns out that one of the requirements was -- they are all on one floor, they have people, they
3 have two or three IT people, and the auditor said you need to hire an IT company -- another IT
4 person to audit what you are purchasing for IT to make sure you are getting value for what you
5 are purchasing.

6 Well, that seems to be more how you run your business than being fully disclosing to the
7 public as to what the results of your business are. So there seems to be blurring of the line
8 between let's do regulations that avoid -- we, on the other hand, we have had just several
9 instances in the last several months where this disclosure as a result of has helped us to avoid
10 companies that we might otherwise have invested in if we didn't have this disclosure. So I am
11 not saying disclosure isn't important and valued, it is just that I don't think one size can fit all.

12 MR. THYEN: Thank you. I am curious, Thomas and Jane, do you have a similar view
13 or do you vary in terms of global competitiveness and the different markets and
14 how the markets support different cost structures and what the regulation burden in the United
15 States does to your judgments on how you invest in companies?

16 MR. RUSSO: One of the central points I think that Jane made was the concept of the
17 privilege of the public market. And I would just spend a second on that, because in the United
18 States historically there has been no federal corporate law. Sarbanes-Oxley has implemented, for
19 the benefit of investors I do believe, some best practice proposals and requirements. I think
20 whistle blowing, I think independent auditors, independent -- and audit committee staffed with
21 financial experts, independent directors as a percent of total. The types of suggestions are
22 moving towards what looks like a national standard for corporate law, but it hasn't been that way
23 in the U.S. historically.

1 So public companies can go public with a Delaware charter or a Rhode Island charter or a
2 Connecticut charter, and so they have the ability to shop for where they want to participate. And
3 so the concept that all companies are burdened across the financial markets similarly once they
4 access public capital, I don't necessarily share that point with Jane. I would say that I personally
5 don't necessarily feel we need a two-tiered system. I simply think we need to get the calibration,
6 to borrow someone else's words, proper for both tiers. I think companies should be treated to
7 the knowledge that what standards they are asked to deliver to is certain, and it should relate in
8 some way to the test for the financial audit. I quite like Jane's comment, though, about
9 connecting the internal control to the risk reduction in terms of fraud. I think it's very important
10 and she made a good point there. But I think there is an example that would strike me as ironic
11 about the two tiers that we are considering. Enron and let's call it Refco, were once large cap
12 companies. They are now small cap. And if we allow them, since they have fallen from grace,
13 as they become small cap then to have a lessened standard of control, we really have put the cart
14 before the horse. The irony, though, is I suspect that Refco probably could have signed off on
15 404, and, yet, we have a terrific example of misleading financial statements and a great fraud.
16 And so, the fact that there is a large cost associated to get to outcomes that may be too precise
17 doesn't necessarily protect us against the frauds.

18 And my last point about sort of the smaller companies, this may not necessarily be
19 required but the smaller companies being historically more the source of fraud, which is I think
20 the point of one of the studies that you cited. I just suggest that that might be that 10b-5
21 violations which are typically one way you measure corporate misconduct arise often in the sort
22 of broken IPO world, and they tend to be smaller companies. So I am not sure that the conduct
23 of smaller companies on an ongoing operating basis is necessarily more fraud inducing. But,

1 certainly, the area of litigation that would pursue that has been related to smaller companies that
2 have come public and then stumble.

3 MR. THYEN: Jane, do you have a view that you care to share? I mean, you don't have
4 to.

5 MS. ADAMS: I would just observe that different governments impose different
6 compliance costs whether it's in the area of social benefits and the environment is evaluated and
7 that the company, that the company is operating in.

8 MR. THYEN: Thank you.

9 MR. WANDER: Yes, Leroy?

10 MR. DENNIS: This question really for anybody. I think I noted on my notes here that
11 nobody here invests in micro cap companies, and so my question would be: Why is that? And
12 if 404 --when 404 is adopted for those companies under the current law and fully implemented,
13 would that change your opinion as to whether to invest in those companies?

14 MR. RUSSO: I don't think any of us can effectively deploy capital, the capital that we
15 manage in that arena, so it's really the lack of the ability to meaningfully commit capital that
16 keeps me from that area, not the question of governance or transparency or accuracy of financial
17 statements.

18 MR. DENNIS: Is that because -- you mean because of the rules that you put in place
19 when you raise that capital?

20 MR. RUSSO: No. It's just -- it's just
21 hard to commit capital if micro cap is defined to be less than 200 million --

22 MR. DENNIS: Our definition is less than 100 million.

1 MR. RUSSO: --100 million. The math just runs into this burden, if you put \$10 million
2 to work in the company, it is 10 percent of the capital structure. You have insider trading
3 regulations that trigger at that point and it is only 10 million on 20 billion of gross and 5 billion
4 of total and 3 billion for us. So you just can't discharge money.

5 There are people who invest in that area with dedicated pools. I don't know whether --
6 they should probably have the same security that Jane seeks, that the control systems are robust.
7 It is just a question of what degree of materiality ought to do because they have to file financial
8 statements that comply with SEC regulation anyhow. This is just another -- a separate area that's
9 auditing control, but they still have to comply with all the financial audits and requirements of
10 SEC filing, so...

11 MR. DAVERN: If I can make a comment, the problem is that it can cost them 10 to 20
12 times more as a percentage of revenue. That's the problem.

13 MR. RUSSO: It will do for sure, and --

14 MR. DAVERN: Therein lies the rub that we might potentially make those companies
15 noncompetitive, and, therefore, is that a good or bad public policy? That is really the tough thing
16 we are trying to figure through.

17 MR. RUSSO: Yes. But you will have -- the security for the investor that they will have,
18 they will have the protection that comes from the standard SEC requirements from disclosure. It
19 is a question on control and how much added value you have there.

20 MR. DENNIS: I guess my question is that if it doesn't increase the availability of
21 capital, it seems like a very expensive cost for not -- I am trying to struggle with the benefit for
22 those people. There obviously are investors out there that invest in these companies.

23 MR. WANDER: Jane?

1 MS. ADAMS: I think that Tom is saying that we are trying to earn a return on investing
2 billions of dollars. We are not retail investors. We are not the small investor who might be
3 trying to deploy effectively and get returns on \$10,000 where that wouldn't be as significant a
4 component of that micro cap company. That retailer investor does need the same amount of
5 controls and the same controls that we would be asking for.

6 MR. RUSSO: There is another observation. In that particular environment there
7 are often companies that drop in and come out of that classification, so it is not necessarily that
8 they are all small IPOs that are just sort of getting traction, sometimes they are large companies
9 whose shares stumble badly, they drop into the category of micro cap and can resurface again.
10 That's an aside.

11 MR. CLOUTIER: Herb, I would like to just ask a general question of the panel: Are all
12 of them strictly long-term investors or do any of them in their funds run a short position on
13 stocks?

14 MS. ADAMS: We are -- Maverick takes positions both long and short. We would say,
15 though, that we are long-term investors, will hold our positions for considerable amounts of time.

16 MS. DOLAN: Herb, I have a question for the panel.

17 MR. WANDER: Why don't we let Tom and Tom answer.

18 MS. DOLAN: Okay.

19 MR. DUNCAN: Well, I was just going to say we are strictly long only. We try to be
20 very long-term investors. It is not unusual for us to hold a stock five to ten years, and try to get
21 to know our managements well, which is really the risk control factor that is most important to
22 us.

23 MR. RUSSO: Exactly the same.

1 MR. WANDER: Janet -- oh, I'm sorry. You can continue, Rusty.

2 MR. CLOUTIER: Okay. Just a follow-up question. Maybe a follow-up comment is
3 that the two of you that are long-term investors, made the comment that you look at the
4 management and look at the companies very carefully, just really kind of interests me versus
5 someone who is on both sides of the equation.

6 MS. ADAMS: I think you've reached a conclusion that is not one that I would agree
7 with. We will both take -- when we take a long position in a company, we will take that
8 position on a long-term basis. We believe, as Tom does, that it's incredibly important to know
9 your management. I would just add that knowing the management and knowing that there is a
10 huge macro story and what the fundamentals are do not eliminate the risk that that company will
11 have to restate because they have inadequately invested in the financial team and are
12 not in compliance with the requirements.

13 MR. RUSSO: Herb, at the start, you asked whether there were some observations that
14 were not directly on point but also impacted our view of the world and money managers.
15 Can we chime in on a couple of those?

16 MR. WANDER: Certainly.

17 MR. RUSSO: Okay, good. I have four, and the first one is an expression of the possible
18 cost of the haste to Sarbanes-Oxley, so it was quickly drafted and responded to specific items of
19 misconduct. So one of them has to do with loans to corporate officers. And WorldCom, I think,
20 sort of drove that point because the chairman, CEO, may have had \$400 million of loans
21 supporting timber investments off the company's books, and that is egregious. But in eliminating
22 the possibility of those loans, one of the great incentive compensation schemes that had

1 been designed by several companies that were very long-term minded was that management,
2 senior management above a certain rank, were required to own stock.

3 And they don't have the money to own the stock so one way to do that would be have the
4 company lend that money to the executives, who then, in turn, buy stocks and then, through that
5 process, become very shareholder minded. And that provision, I think, of Sarbanes-Oxley may
6 have overreached, because to the extent that it is aligning the decision-makers' interest with the
7 owners' interest through actual shares owned rather than option shares, it was a very useful
8 provision. And I think it has been eliminated because of the restrictions against Bernie Evers.
9 So that was an example.

10 I think there is one area that I personally find extremely valuable in investing, and as the
11 SEC may reflect on this from time to time, it is the value derived from segment reporting,
12 operating segment reports are terribly important for investors in companies that have multiple
13 business units, and it has been proposed over time that if the information were valuable, investors
14 could search that out on themselves and that the segment reports are, in fact, a burden that
15 doesn't have much benefit. I think there is a tremendous benefit that come from segment
16 reporting.

17
18 A third point I would stress is in the world of information disclosure, there seems to be a
19 trend, and Jane mentioned in the foreign world that the information flows too slowly and, indeed,
20 foreign companies often have semi-annual reports, not quarterly. But I fear that in trends within
21 disclosure requirements that we may end up as investors facing instantaneous disclosure. And so
22 the SEC -- sort of materiality. You end up moving towards a world where any untoward event
23 needs to be disclosed to comply with FD upon knowledge. And I think that burden to the

1 investment community would be very high. Because many events that are so disclosable work
2 their way out during periods of time, whether it is a quarterly cycle or semi-annual cycle. But
3 the move towards more instantaneous and continuous disclosure, I think, would burden
4 companies and lead them to focus on ever shorter term issues, whereas the real money is made
5 by folks on long-term issues. So I don't know whether that's an area of purview for the SEC, but
6 it would be something that I would think would lead investors in the wrong way, the right way
7 being to focus on longer term and important issues. Those are three cited ideas.

8 MR. WANDER: We have a couple more minutes, so if there are any other questions or
9 comments from the presenters.

10 MS. DOLAN: Herb, I have a question.

11 MR. WANDER: Sure, Janet.

12 MS. DOLAN: We seem to have division of opinion among the panel, so I would just
13 like to hear them respond to the proposal of if we have a smaller company that has invested and
14 paid for and received a 404 certification without material weaknesses in year one, then could we
15 let that company have one, two or three years when they don't have to do a full 404 again and
16 then perhaps do it periodically?

17 And we indicated earlier on that we were looking at that as a possible way to spread the
18 cost and the efforts out for the smaller companies and reduce it for them. And two of our
19 speakers have suggested that they would -- that they would consider that, or at least they are
20 urging us to consider that. We got some concern from the audit firms that that would not be
21 workable because investors would not feel comfortable investing in companies that didn't have --
22 if 404 was required, didn't have it every year and that they would basically, auditors could well
23 be exposed to shareholder litigation and other matters for not having done it every year even if it

1 wasn't required. So I am interested in these investors' views of how would that view that?
2 Would they feel that they had adequate both disclosure and protection if it was fully clear that
3 this was a periodic event and not an annual event?

4 MS. ADAMS: We would prefer that the internal controls be evaluated, tested and
5 reported on an annual basis.

6 MR. DUNCAN: I don't think there is anything magical about an annual review. I think
7 changes that occur in internal controls should be reported on at least annually, if not more
8 frequently. But if these procedures are in place and the general audit verifies that they are
9 working, I don't see why they should have to be reverified every year.

10 MR. RUSSO: Yes, I think that's a very good point, though, absent change. If there are
11 changes, then subject that to disclosure. But, clearly, the auditors' reluctance to sign off in a
12 world that you envision which has some holiday from annual full audit for Sarbanes-Oxley
13 Section 404 suggests that they feel that the standards to which they are held are too tight or else
14 inconsistent with the standards that they operate on under financial accounting. I think a lot of
15 this would be cleared up if you could somehow, through the PCAOB and the SEC, come up with
16 a more articulate form of calibration. And there you will end up with year one probably being
17 less costly and ongoing reviews being less costly, in any event. So I think it seems like there is
18 a very stark tension growing between the companies and their auditors over how
19 much work the auditors need to do to comply, and that, I think, can be addressed through
20 communication, like you have presented it, but really hasn't been forcefully embraced yet.

21 MS. DOLAN: Thank you.

1 MR. WANDER: Any other comments, suggestions? Comments from the presenters,
2 concluding remarks or observations? I know you have all been terrific and we greatly appreciate
3 your sharing your time and your really considerable thoughtfulness

4 MR. RUSSO: Thank you very much.

5 MR. WANDER: Our next panel doesn't begin until 3:15, and so I suspect we should
6 take a break. I guess everybody on the phone, you should put it on hold and look at your new e-
7 mails for 15 minutes. Put it on mute, please, and we will reconvene in 15 minutes. And I want
8 to again thank our presenters.

9 (Recess taken.)

10 MR. WANDER: We are going to resume our session and go to our second panel. We
11 have four presenters this time: Martin Whitman, Judith Vale, Gerald White and Bill Miller. We
12 will follow our sort of informal procedure that we have done so well with, I think, so far.
13 I would like to start off with Martin Whitman of Third Avenue Management. We are
14 delighted to have you here.

15 MR. WHITMAN: Thank you. Nice to be here. It's funny, I wrote a book in 1979 and
16 then Wiley induced me into updating it. It will be out next week. The gravamen of the changes
17 are there has been a virtual disclosure revolution. I thank you, I thank the plaintiffs' bar, I thank
18 a lot of people, but for us disclosure has never been better, more complete, more akin to due
19 diligence, in terms of what we do. And we, quite simply, are long-term investors, buy and hold,
20 and our mantra is if we are going to in common stocks, they are going to be safe and cheap,
21 which I need not expound on further. But for our constituency, things have never been better.
22 They are terrific.

1 To get to the topic at hand, though, disclosure can never meet the perceived needs of
2 short-run stock market speculators, and it's absolutely stupid for you people to try. A short-run
3 stock market speculator is anyone, individual or institutional, who thinks they are vitally
4 influenced by day-to-day stock market fluctuations. When I went in the business, for many,
5 many years, the mantra was: You get disclosure and what you did with it was your business. If
6 you didn't want to use it, it was your business. Nobody spoon fed investors. Specifically, I don't
7 think there is anybody in the world with an IQ over 75 who thinks financial accounting ought to
8 tell them the truth. What it does, it's absolutely essential, and what it does is give the serious
9 analyst objective benchmarks, probably only the objective benchmarks he would ever have,
10 which he can use to determine his version of the truth. But you can't take a rigid system,
11 whether it's the Internal Revenue Code or statutory accounting for insurance companies, or BD
12 accounting or GAAP and try to say it's going to be truthful and accurate or that there is a primacy
13 of anything, whether it's cash flow or earnings. It's just not -- for you regulators to go down that
14 path, it's just endless and you are never going to satisfy that constituency.

15 Indeed, just a shorthand, I think disclosure, from your point of view, ought to essentially
16 be directed towards meeting the needs of long-term creditors. That's very different, much more
17 so long-term creditors rather than stock-market speculators. Last month I read an interesting
18 book by Milton Friedman, who leaves a lot to be desired, but he talked about the importance of
19 markets and the necessity for voluntary exchanges, which is what markets do. Of course
20 Professor Friedman doesn't know anything about corporate finance, but in corporate finance, we
21 have certain activities that are the equivalent of voluntary exchanges and certain parts of
22 corporate finance where it is per se coercive. In voluntary exchanges with just a market, there's

1 open-market trading. There is some cash tender offers, there's voluntary exchanges of securities
2 who are in distress, reorganizations, of course.

3 Also, there are a tremendous number of things we do in the financial community that are
4 basically coercive on security holders; that's mergers and acquisitions where the requisite vote
5 coerces all stockholders; in effect, it's going on with the deal. There are going private tender
6 offers that are coercive because you have put it out of market. There are Chapter 11
7 reorganizations. Indeed, there are trust indentures where any provision except the money
8 provision can be coercive, that a money provision under the Trust and Venture Act and every
9 venture the same, is voluntarily because you can never force a bond holder to give up his right to
10 a money payment outside of a court proceeding.

11 Now on the specific topic of small cap companies as a predicate, I don't think small cap
12 companies should be coerced into complying with Sarbanes-Oxley at all. It is just a waste. In
13 addition to being an investor, I am also the financial principal on an audit committee and we
14 have been, I must say, extraordinarily successful investors for over 50 years, and all the time our
15 basic reliance was on financial accounting. We never messed with managerial or cost
16 accounting and it never was a problem. 404 has to do with managerial accounting, internal
17 controls. We function extremely well without paying any attention to it, and we don't think
18 CEO's and CFO's ought to attest to things that can never be truthful; to wit, GAAP financial
19 statements.

20 Rather than having small cap required to obey Sarbanes-Oxley, I would propose we use a
21 crazy theory, the efficient market, give them enough disclosure and the market will take care of
22 it. And what happens is small companies as defined, however defined, can opt out of Sarbanes-
23 Oxley, provided there are comprehensive disclosures in 10-K's, 10-Q's of the disadvantages to

1 the stockholders, present and potential, that will be visited on them if they invest in companies
2 that don't give them the protections of Sarbanes-Oxley. I would have other proposals along that
3 side for foreign issuers and so forth.

4 My closing comment is: I think this is a lot more important than just me money
5 grubbing. We are really screwing up the capital markets with things like Sarbanes-Oxley, things
6 like discouraging any foreign issuer that doesn't need the capital markets from ever subjecting
7 themselves to United States' jurisdiction. From a public policy point of view, please rethink in
8 all areas what you are doing long term to the U.S. capital markets, one of the greatest resources
9 we have. Thank you.

10 MR. WANDER: Thank you very much. We now will open it up for questions and
11 comments from committee members.

12 MR. DENNIS: I just have one question: Can you define "small cap companies" as you
13 define it?

14 MR. WHITMAN: Well, I see in the papers you had two definitions. I would have
15 something that works; say, a market cap under a billion. Whatever works. It's a question better
16 directed towards Judy who runs a small cap fund and would have a good idea of what it is. I
17 wanted to get into the principle rather than -- the cost now is just prohibitive, you know. They
18 ought to be guided by -- it really doesn't benefit -- you know, without benefit for investors. I
19 think, you know, as I put it, Sarbanes-Oxley was designed to prevent WorldCom, Enron,
20 Adelphia; that's not percent of the issuers, believe it or not. It's certainly none of
21 the issuers with which we are involved.

22 MR. WANDER: Bob?

1 MR. ROBOTTI: Hi Marty. One of the things you mentioned was exemption from
2 Sarbanes-Oxley and I guess I'm on the corporate governance committee and, you know, they
3 were concerned about independent directors, audit committee, those kinds of issues. Are you
4 talking broadly all aspects of Sarbanes-Oxley? Of course we know the other component that
5 seems more contentious is 404 and the cost associated with 404 and the benefits of that?

6 MR. WHITMAN: I particularly focused in on the cost of 404 and the attestation by
7 chief executive officers and chief financial officers. You know, they are attesting, that I could
8 see, you know. I used it in court for the plaintiff's bar, they are attesting to things that can't be
9 attested to, if you were engaged in -- if you were dealing in reality.

10 MR. WANDER: Kurt?

11 MR. SCHACHT: Hi Marty, Kurt Schacht from CFA Institute. Thanks for being here on
12 a rainy afternoon. Just on the question of internal controls, is it your view that small cap
13 companies, public companies do not need internal controls or we just don't need any sort of
14 external verification of those controls?

15 MR. WHITMAN: Of course they do. But I think, you know, for my purposes, they
16 always had it under GAAS, generally accepted accounting standards. You need audits; you
17 need to direct towards GAAP. You know, we have had GAAS, we have had things, and
18 that's thousands of thousands of investments. I don't know we were ever involved with internal
19 controls.

20 In fairness, I've got to say that most of our investments happen to be in real estate
21 securities and financial institutions. We don't do much high tech. We don't do much in the old
22 economy, manufacturing companies. We do it in distress, we don't do it in common stocks. So,

1 you know, from where we sit, internal – for 50 some years internal controls were plenty good
2 enough before 404, and I don't know if 404 would have prevented Enron.

3 MR. WANDER: Yes, Leroy?

4 MR. DENNIS: Marty, you just mentioned something that sparked my interest and that's
5 the financial institution investments you do. We heard a lot of testimony from bankers about the
6 over regulated burden they have between the different safety and silence regulators they deal
7 with, and then if they are a bank holding company dealing with the SEC. I wonder if you could
8 comment from an investor's standpoint as to what you see from a banking investor?

9 MR. WHITMAN: Okay. You can take this to the bank: Financial institutions don't
10 work unless they are strictly regulated, and I give you the Investment Company Act of 1940, as
11 amended. Were it not that strict regulation, we would have had a lot more Bernie Kornfelds and
12 Viubes and what happens, our great marketing tool happens to be that we are strictly regulated.

13 I really think sociologically there is no paper-pushing profession, which is what financial
14 institutions are, that don't have to be heavily regulated. I say it should be intelligent
15 regulation, like the Investment Company Act of 1940, but I don't think the system unregulated,
16 whether it's banks, insurance companies, investment companies, really would function well
17 either for investors or for the economy, unless they're subject to meaningful, intelligent
18 regulation.

19 MR. WANDER: Yes, Jim?

20 MR. THYEN: Marty, I am Jim Thyen. Would you please expand a little bit more on
21 your comment "meet the needs of long-term creditors"? You said: Meet the needs of long-term
22 creditors, as opposed to, investors.

1 MR. WHITMAN: If you are a long-term creditor, you analyze the company on the basis
2 that the company within itself will have the resources to meet the cash service on the debt or the
3 company will remain credit worthy enough to access capital markets. And I will tell you, we
4 basically, let's say, we're 90-some percent in common stocks though we analyze as if we were
5 long-term creditors.

6 I think it's a good rule of thumb. Certainly you ought to get off the idea that you are there
7 to meet the perceived needs of the short-run stock market speculators. You are only there in the
8 sense that outside this disclosure area, the SEC is perhaps even more importantly charged with
9 the maintenance of free, fair and orderly markets. Who can say disclosures doesn't impinge a
10 little on it, but basically I think you are better served in coming up with regulations, if you do
11 things from the point of view of the long-term creditor. In updating my book, I went through --
12 the first edition was 1979, I went through every SEC annual report update and improvements in
13 disclosure from 1979 to date. They have been fantastic and remarkable, only they were not the
14 fish you want.

15 MR. THYEN: Thank you.

16 MR. WANDER: Other comments or questions? Anyone on the telephone?

17 MR. BOCHNER: Steve Bochner has a question, Marty, thanks. I think a lot of your
18 comments went to and the cost burden. If you were to pick a number two or three, if I could ask
19 you that, if you were in our seat and had this fairly broad job to do about looking at the
20 accounting and governance and disclosure and the capital formation, is there something else that
21 you would focus in on once you thought that you had resolved the 404 cost issue? And I am
22 talking about some of the things that we focused on, disclosure, board independence, materiality;
23 you know, we have such a broad mandate here, or is 404 really the big issue?

1 MR. WHITMAN: That's a big issue. You know, I think disclosure is so good, I am sort
2 of a cynic. It's a real oxymoron, "board independence," I mean, is that going to happen?
3 It's a pipe dream. Management runs companies and the nominating committee nominates boards
4 and basically I think it is going to remain very hard, no matter what SEC or any other authority
5 does to get boards who aren't relatively close to management. That's just, you know, it is not real
6 world. I wish it were. Or, you know, as I say at one point, there are various forces that impose
7 disciplines on markets and there are myriad markets. Competition imposes discipline for the
8 plain, passive investor. Government regulations maintains orderly markets led by financial
9 institutions. The market for management compensation is, of course, governed by
10 Boards of Directors. That's why you get these unbelievable excesses, and I don't know what you
11 can realistically do about them.

12 MR. WANDER: Other questions, comments?

13 MR. CLOUTIER: Rusty Cloutier, Marty. I wanted to follow up with the comment that
14 you made a couple of times about swing investors. I take it you are talking about people who are
15 in the market, charting it, and moving very quickly, like a hedge fund; and I get the feeling that
16 you are making a comment that it is the not SEC's responsibility to give them instantaneous
17 information so they can try to make these short-run, swing profits. And then a second question I
18 would like to pose which is a little different, to follow-up on the question about banks: Do you
19 think the banks were properly regulated before 404 or that they needed additional regulation on
20 top of what they have today, as far as reporting goes? So kind of two questions.

21 MR. WHITMAN: What was the first one again?

22 MR. CLOUTIER: The moving of short sales and very quick in and out of the market.
23 You made that comment a couple of times.

1 MR. WHITMAN: When you read my update, I have the risk arbitrage exception.
2 Again, when I talk about our style of investing, we are always the last to know. We don't get
3 superior information or earlier information. We use the available information in a superior
4 manner, and I had meant before, I meant away from me the SEC has a big charge to maintain
5 free, fair and orderly markets, which means, I would suppose, that against that background there
6 is a lot of justification for Regulation FD, even though it doesn't mean anything for our
7 investments.

8 As for the banks, I really don't know. One of the things that happened is what I call,
9 "Thank you Michael Milken." It is corporate lending by banks has never been sounder than it is
10 now, and that goes back at least 300 years. So they may need more discipline in what they are
11 doing in consumer loans, especially mortgage lending, and maybe a lot of governments are going
12 to go bust, but corporations happen to be very sound, corporate lending.

13 I think what happened, for better or worse, is the risks the banks used to take up until
14 about 1990, in things like lesser developed companies, real estate, oil and gas, those risks have
15 now been put on to the junk bond market. So, you know, I don't know what to say except
16 basically commercial banks are doing a very sound job in corporate lending, which I know a
17 little bit about.

18 MR. WANDER: Anyone else? If not, Judy, I would like to hear from you, please.

19 MS. VALE: I am delighted to be here. I head up a team of five people at Neuberger
20 Berman that runs the small cap value product. We are running about \$14 billion dollars, and I
21 think it would be useful for you all to know what small cap means in our universe, which is not
22 at all the universal use of the term. But given the fact that our management style is extremely
23 low turnover, probably averaging something a little less than 20 percent a year for the last five

1 years, implying an average holding period of a little more than five years, and I will also add that
2 a few percentage points by turnover every year are usually due to takeovers, so our turnover, left
3 to our own devices, is very, very low. This almost guarantees that your average market caps are
4 going to look large when you compare against an index which is rebalanced every year.

5 So the average market caps in our portfolios at the moment are on the order of two
6 billion, a little higher. Actually, after the correction of the last week or so, maybe a little lower,
7 but we are not looking at companies that average around the definition that you are using. We
8 certainly are not involved in micro cap companies at all, that is 100 million or less. We are
9 involved in quite a few companies that, perhaps, will go down to the 400 million level, but these
10 do not predominate.

11 At any given point in time, we are probably invested in between 150 and 170 names, and
12 we are looking at a number more. So I would say that we are fairly active in our universe, as we
13 define it, which is a little bit larger in my understanding of how you are defining it.

14 Before I speak specifically about our feelings on Sarbanes-Oxley, I would also like to add
15 that because of our style of management, which has to do with focusing on relatively mundane
16 businesses with very predictable cash flows, we are more focused on cash flow than on earnings.
17 Over the last 15 years that I have been at Neuberger Berman, we have had very, very few issues
18 from an accounting debacle at one of our companies. We are looking at a selection which tends
19 to be more conservatively managed. We look to see conservative accounting practices when we
20 are doing our analytics, so we are self-selecting a group of companies that perhaps would be less
21 likely to try to mislead investors. And perhaps because of this, Sarbanes-Oxley really has not
22 been much of an issue for us, one way or another.

1 Most of our companies are complaining about it to varying degrees, and I would say that
2 if I could generalize the amount that they are expending on compliance, it ranges from a few
3 companies that have said they really didn't have to do that much to be complaint, which is one
4 extreme, and they wouldn't even give us a number, to a handful of companies that claim that it
5 cost them on the order of 5 million. I would say the average seems to be one or two million, but
6 also people are coming up with their numbers differently. Some people are just counting the cost
7 of hiring outside help. Some people are also saying, "Well, my treasurer is spending X percent
8 of his time so we allocate that as part of the cost." So I also can't say that the costs are being
9 figured in any kind of consistent manner and it hasn't been a focus of ours. But I guess our
10 feeling was that for the most part the costs do not seem to be material, given the size of company
11 we are dealing with.

12 The companies that we talk to do more often than not feel it's a burden. They don't feel
13 like they have in a sense gotten their monies worth for the investment. However, on the margin,
14 a number of them have said that specifically with xx, they have found that some of their systems
15 weren't quite as good as they thought they would be, and it's led to new software investments or I
16 don't know what, which made me, as an investor on the margin wonder, "Well, maybe this has
17 more value than they're admitting to." But, again, I can't say that we have done a thorough study.

18 So for us, I guess, I don't feel as strongly as Marty that this is a tremendous burden;
19 perhaps because small cap for me is larger than some of the companies that his company is
20 invested in. But in general, the costs don't seem so burdensome. So what I did before I came
21 was, I actually had jotted down a handful of anecdotes on the basis of companies we have talked
22 to recently, but I think that they are less relevant than the over arching conclusion; simply that
23 for the subset of businesses that we are talking with, for whatever reason, it's an inconvenience,

1 it's costly, it is not crippling. And most companies that we talk to say that their costs will be
2 down substantially next year with compliance. There is still going to be a cost, but they are
3 expecting it to be a lot less.

4 MR. WANDER: Okay, thank you. Questions? Kurt?

5 MR. SCHACHT: Thank you for being here. Just a quick question. You have
6 articulated your perception of the cost side of the equation. As an investor in these companies,
7 ranging from two billion down to the 450 million market cap, what's the benefit to you as an
8 investor, in terms of should they all have internal control? Should they all have the same
9 level of external verification?

10 MS. VALE: I guess I also feel a little cynical in my role as a professional investor, and I
11 don't think that by itself, 404, as I understand it, or even Sarbanes-Oxley, would make or break
12 an investment decision. We are looking for businesses that have certain characteristics, and what
13 we are looking for is so clear cut and definable, either companies have it or they don't. You
14 know, consistent free cash-flow generation and this sort of thing.

15 We would not place a tremendous amount of weight on whether or not -- if, for example,
16 you were to exempt a certain number of companies from compliance, I don't think it would really
17 make a huge amount of difference to us, although we would certainly take note and perhaps look
18 a little bit more carefully at the financial statements to see whether or not they are less
19 conservative than we thought they were. And probably it would also bring up a discussion with
20 the management as to why they chose not to comply, I mean, if it were some kind of an option,
21 but I don't think it would a make or break.

22 It seemed to me that the painfulness of the compliance was very dependent on the
23 complexity of the business and the business models. And, for example, a little company that we

1 are involved with, that has a very mundane business of running hair salons, the drove them
2 crazy because they are literally involved in thousands of salons that are scattered all over the
3 place, and so for them to do compliance meant, it was a much bigger deal than a
4 company that has a different kind of a business model, where things tend to be more focused in
5 one place.

6 So I think, as an investor, it is not a huge benefit to us, although to the extent that they are
7 going through this, I was pleased to hear from a couple of companies that they did think that
8 their systems, as they examined them very, very closely, could use a little bit of improvement
9 and they were making those investments.

10 MR. WANDER: Other questions. Jim?

11 MR. THYEN: Yes, I am Jim Thyen. Do you have opinions that you care to
12 share in the other areas of our fact-finding: Capital formation, governance and disclosure and
13 accounting standards?

14 MS. VALE: I am generally all for disclosure, but I think that I am also in a similar
15 camp with Marty, that because of the way we run money, we are the last ones to know anything,
16 and it really doesn't matter. We are investing in businesses that we think are fundamentally
17 good, and to the extent there's some little item of news --"Oh, no, the company is missing the
18 quarter" --everybody knows it before us; the stock is down 20 percent. We usually use it as an
19 opportunity to arbitrage our time frame with that of the short-term investor. So in terms of the
20 timeliness of disclosure, it is not that important for us.

21 And I feel that in general the quality of earnings are that we are looking at or the quality
22 of the accounting seems to be pretty good. Now I feel like there have been a lot of -- I have

1 been in the business a mere 20 years, but it seems to me that standards have certainly been
2 improved, which is a huge positive.

3 MR. THYEN: How about capital formation, the impact of Sarbanes-Oxley on that
4 relative to other alternatives in the world and global competitiveness? Any opinion there?

5 MS. VALE: I suppose on the margin it does function a little bit like a tax on
6 profitability, to the extent that it is significant and relative to a company's size, and that it would
7 be on the margin. It would make them, to the extent their earnings are less, presumably it would
8 affect their market capitalization or access to capital on the margin, so there is a cost involved
9 most definitely. And I think that were it possible to make compliance less onerous in some ways
10 -- I mean, this is being put together fairly quickly, and as we think about it more you may figure
11 out a way to reap 80 percent of the benefits with 20 percent of the cost; you know, that would
12 certainly be a positive because we don't want to burden managements.

13 One of the costly aspects of compliance, which doesn't directly have to do with dollars
14 and cents, is just the amount of human focus and time that has gone into compliance with smaller
15 management. In a sense that bothers me more sometimes than the dollars and cents, because I
16 wonder if they are really being taxed to the point that they are not focusing on the things they
17 should be focusing on in their competitive environment. So there are probably also hidden costs.

18 MR. THYEN: Okay, thank you.

19 MR. WANDER: Any other comments, questions? Thank you, very much, Judy, and
20 let's move on to Bill Miller from Columbus, my old state.

21 MR. MILLER: Thank you. Good afternoon. Mr. Chairman and Members of the SEC
22 Advisory Committee and smaller public companies, my name is William Miller. I am a senior
23 investment officer for the Ohio Public Employee Retirement System. The Ohio Public

1 Employee Retirement System is more than a 64 -and-a-half billion dollar fund, serving three-
2 quarters of a million Ohioans, making the system the tenth largest state pension fund in the U.S.
3 Yes, we do invest in both small and large public companies.

4 We appreciate and thank you for the opportunity to provide input to this advisory
5 committee. Our executive director, Ms. Lori Hacking provided this committee with our views in
6 a letter dated August 31st, responding to 29 questions from the committee. I would ask that that
7 letter be placed into the record of this meeting. Our view, as stated then, remains unchanged. To
8 summarize, we believe that all companies publicly traded on U.S. exchanges should comply with
9 Sarbanes-Oxley requirements, regardless of size or whether U.S. or foreign firms, at the same
10 time. Many U.S. firms complied with the Sarbanes-Oxley requirement at year end 2004. The
11 results of compliance appear positive. The results of non-compliance speak for themselves.
12 Look at the recent press, New York Times, the Wall Street Journal on Refco.

13 It is our understanding that smaller companies had a later deadline to comply with
14 Sarbanes-Oxley. The deadline had been pushed back several times and each time, I guess, the
15 SEC had accommodated and hit the snooze button. To our dismay, just recently, on September
16 21st, the SEC extended the deadline even further, to as late as 2008. Continuing to hit the
17 snooze button and postpone compliance with Sarbanes-Oxley impairs investor confidence in
18 U.S. markets. U.S. investors rely on audited financial information to make informed investment
19 and comparative investment decisions. To the extent the financial data is wrong or fraudulent,
20 investors, whether large or small, are harmed and lose confidence in U.S. capital markets. A
21 lack of confidence translates into greater volatility and a higher cost of capital, retarding
22 economic growth and employment in the United States.

1 We ask that the SEC reconsider and roll the compliance requirement back to 2006 and
2 that any further relief be on a case-by-case basis, by petition to the SEC for a further deferred
3 compliance deadline. When not in compliance, such firms should disclose if they are not in
4 compliance, similar to the Surgeon General's warning for smoking, something like: This
5 company is unable to comply with the enhanced financial testing and recording requirement
6 under Sarbanes-Oxley and may be subject to material financial restatement, which could result in
7 significant or total loss by being not in compliance. It should be considered. This would
8 disclose to the public that the company may be prone to restatement and the investor could be
9 materially harmed. Again, look at what just happened with Refco. U.S. companies compete in
10 a global arena. U.S. firms compete with foreign firms who are not compliant with Sarbanes-
11 Oxley financial requirements.

12 Those financial firms listed on U.S. exchanges are siphoning capital from those U.S.
13 companies, affecting U.S. company growth, competitiveness in employment. The bias in favor
14 of foreign companies by giving them exemptive relief versus U.S. firms that do comply is just
15 clearly wrong. The objective should be to encourage firms to comply as quickly possible. The
16 SEC should also be proactive and work with other government agencies and smaller companies
17 and should develop incentives to get all U.S. companies into compliance. Let's be creative. Let's
18 find solutions to push U.S. firms into compliance to maintain their international compliance.
19 Lowering the bar has long run negative implications. Thank you.

20 MR. WANDER: Leroy?

21 MR. DENNIS: Thank you. I just have two questions. One, do you invest in micro-cap
22 companies, as we have defined them?

23 MR. MILLER: No.

1 MR. DENNIS: Do you invest in small-cap companies as we have defined them?

2 MR. MILLER: We invest in Russell stocks.

3 MR. DENNIS: Okay. So that would include some small-cap companies, then?

4 MR. MILLER: Yes.

5 MR. DENNIS: Then, I am curious by your comment that, with your disclosure, which I
6 absolutely tend to agree with, something like that I think is appropriate, whether it's on a star
7 symbol or a ticker symbol or whatever it may be, but I am concerned by the implication that just
8 because a company does SOX, that they are going to be less likely to have restatements. I am
9 not sure I have seen the evidence that that will be the case, and I am interested in your thoughts.
10 I am very concerned about the perception that because a company goes through SOX that they
11 are going to have perfect controls and no fraud and no restatements.

12 MR. MILLER: I would agree with you. I think there ought to be some type of
13 education to investors to recognize that even with SOX you are going to get restatements.
14 However, I don't believe you are going to find the same magnitude as you would find, that are
15 currently occurring when you don't comply.

16 MR. DENNIS: The other question I would ask you is, you know, especially in dealing
17 with micro-cap companies, to the extent they restate, I would assume that really doesn't have an
18 impact on investor confidence like, obviously, a larger company.

19 MR. MILLER: Well, if you were to look in the press every day and find that half a
20 dozen micro-cap stocks or small-cap stocks were continually restating due to fraudulence or lack
21 of internal controls, I think that would start having a negative impact on the overall confidence of
22 the market. I am not sure people are going to differentiate and say, "Oh, you know, this fraud,

1 that's prevalent manipulation, it's only with the small, very small stocks.” You are going to
2 impact investors.

3 MR. DENNIS: Okay, thank you.

4 MR. MILLER: And I can see press making--

5 MR. DENNIS: I certainly would agree with you on the press comment.

6 MR. WANDER: It's interesting, you indicated that any publicly held company, you
7 think, should go through the SOX. What we have found, dissecting the sort of data, is that there
8 are some 4,000 to 13,000 companies on the pink sheets who, frankly, are not necessarily
9 required to comply with anybody's requirements, and just sort of, I think, even to us, who were
10 sort of supposedly in the know, were unaware of the large number that really don't have any
11 requirements at all, at least to be listed on the pink sheets. They don't have to be in compliance
12 with the SEC reporting requirements. Now you don't invest in them, so it's probably out of sight
13 out of mind.

14 MR. MILLER: Yes.

15 MR. WANDER: But it's an awful large percentage of the public companies. Not very
16 much in terms of market-cap, it's probably less than one-tenth of one percent of the total market
17 cap. Other questions, comments?

18 MR. BOCHNER: This is Steve Bochner, again. Thanks for your testimony.
19 You mentioned Refco, I don't know a lot about that situation because it just made the news,
20 but it looked like a New York Stock Exchange company that presumably went through 404 and
21 had a loan that was hidden; do you think that the 404 process will or should uncover sort of
22 senior management deceit like that? Because it sounds like you were using it as an example of

1 why 404 ought to apply to small companies and it doesn't seem to me to be relevant to that issue,
2 so I am curious about your views as to whether 404 could really prevent fraud of this nature?

3 MR. MILLER: I would have hoped that 404 would have picked it up, but it didn't
4 comply. I mean, looking into just what it says here in The New York Times, when it went
5 public, Refco was forced by Sarbanes-Oxley to report significant deficiencies in its internal
6 controls, including inadequate finance staff -- including an inadequate finance staff. Investors
7 did not care. It turned out that such deficiencies can be very real and very costly. It should have
8 been a warning bell and the audit committee should have pursued it.

9 MR. DAVERN: This is Alex Davern here. If I could hang on to Steve's point, one of the
10 things that's bothered me, and I'm curious as to your opinion on this, all along: If a public
11 company falls under another public company, and one of the things that I learned when I went to
12 accounting school and audit school and so forth was that we were taught that internal controls
13 don't detect collusion by senior executives in committing fraud -- this goes back to the point
14 Steve was making earlier on.

15 I am personally very concerned about the perception that is, I think, fairly prevalent upon
16 the investment community that 404 will prevent frauds of this nature, whether its Enron or
17 WorldCom or Refco, whatever. I am curious to hear, there was something from the American
18 Association of Certified Fraud Examiners which showed that internal controls are among the
19 least effective methods of detecting fraud by owners and executives that is committed by
20 collusion because of their ability to override these controls. And this has been one of my
21 personal efforts on this committee, to try to make sure that the right perception is communicated
22 now. It's my belief that 404 will be relatively ineffective in preventing Enron-style corporate
23 fraud. My big concern is that when we have the next major Enron type scandal and that

1 company has a clean 404 opinion from auditors, 404, that that will do more damage to investor
2 confidence than we had before.

3 I will get to my question. My question really is: Do you think investors have a belief
4 that fraud will be permitted by 404, is my first question. And then my second question is: I
5 know you don't invest in microcap stocks, but if the consequence of applying 404 to microcap
6 stocks was that the percentage of revenue and profits was going to be so high that it would cause
7 these companies to de-list? Do you think that that's the right public policy mode and the right
8 balance of decision making here, that it's better to have these companies de-list and not be a
9 factor to public funds than it is to scale 404 to make it more practical for their case?

10 MR. MILLER: Okay. There were two questions, but I am going to answer three, if I
11 could?

12 MR. DAVERN: Absolutely, fire away.

13 MR. MILLER: The first relates to 404, and your point that its the least effective, but
14 what you didn't tell me was it was ineffective. In other words, it can have the ability to identify
15 where there can be some problems.

16 MR. DAVERN: Well, perhaps I can check the data to help you put it in perspective.
17 Let's take, techs are responsible for 51 percent of detached; internal audit is responsible
18 for 23 percent; external audit for 27 percent -- that's the traditional external audit we have always
19 known. Cases detected by accidents are 12 percent and internal controls are 6 percent.

20 And one of the perspectives, just to share, just to get some of the feedback from having
21 others look at the problem is that for a company, I represent National Instruments as the CFO,
22 now we are not going to benefit any from what's on the table, we're clearly a large public

1 company It cost us \$5,000 to implement a whistle-blower provision. It costs us 3-and-a-half
2 million dollars to do 404, so that's just some other data to share with you.

3 MR. MILLER: What you have told me does not dissuade me from my perspective,
4 because I am not sure whether your data is pre-404 or post-404, and I'm looking at this data and
5 I'm saying, well, all right, I've got internal audit and external audit; about 50 percent is detecting
6 the issues. So that's a positive. If you are telling me to unwind 404, what message are we
7 sending?

8 To answer what I am going to call the ancillary part of your question, I think we should
9 look at Sarbanes-Oxley in its entirety, because by putting independent board members on the
10 audit committee, forcing that independence, and looking at what's happened in the past,
11 particularly with regards to the governance committees, and the nominating committees, as well
12 as audit, I think one of the things that -- and I serve on several audit committees as well -- that I
13 look for is what is the relationship that exists between the CEO and the other members of
14 management that allows them to have independence back to the board so we have adequate
15 checks and balances?

16 I understand the issue of collusion, but when we went through the 404 compliance and
17 we sat with management and several layers of management to go through what were the
18 attestations regarding each of the significant control factors, I walked away with a greater degree
19 of comfort knowing that when we went through the exercise initially in early 2004 and we found
20 deficiencies or gaps, as they are called, and we remediated them, and we went through that
21 process, we, as the board members and then audit committee members, were much more
22 knowledgeable about the issues associated with that firm and felt much more comfortable after
23 the fact.

1 Now, granted we did spend more than \$90,000, but at the end of the day we felt very
2 comfortable that we were in very good shape for our investors.

3 MR. DAVERN: Thank you for your comments.

4 MR. MILLER: I guess the other question, the last question you asked was whether the
5 economic balance, with regard to the firms could not comply and they were to de-list. If they
6 were to de-list, then their primary source of funds would be through private market, private
7 equity markets or through the debt markets, and at that point those investors will be able to
8 exercise, I think, the level of control that would be equivalent to Sarbanes-Oxley.
9 So I am not sure you are going to get away from it by de-listing, depending on the nature
10 of who the investors are and how comfortable they are with their money at risk.

11 MR. DAVERN: Perhaps you could come back then to one last question, to the question
12 of the cost, which I think is -- I personally am in favor of all the elements of the Sarbanes-Oxley
13 and I didn't have an issue with when it first came out on the premise that it was going to cost
14 \$90,000, but do you see a point at which the trade off of cost versus the benefit for any size of
15 company -- in other words, if it's going to cost the company 6,7,8, 10 percent of revenue, and
16 then you're saying it should apply in the private or public community, then how do these small
17 companies, what do we tell these small entrepreneurs who are trying to grow a profitable
18 business?

19 MR. MILLER: Well, I think there is a balance.

20 MR. DAVERN: Do we tell them to move to the U.K. or what do we tell them?

21 MR. MILLER: No, we don't, no. We've got to be proactive. We have to figure out
22 ways to get them over the bar, whether it's through financial incentives, in terms of tax credits
23 associated with it or whatever, but we have to be creative in this regard because I think they all

1 have a duty to have a certain level of quality with regard to their internal controls and their
2 financial statements. I think you have to look at the companies based on the facts and
3 circumstances, and their degree of complexity, as well as the type of profitability they have in
4 order to cover those costs. So there is a balance to be struck.

5 MR. DAVERN: Now, a tax cut, if we can get that done, I think you'd have a lot of
6 CFO's who would agree with you there, but I am not sure that's viable in the current budget.

7 MR. MILLER: I would only do it on the incremental portion and have some kind of
8 shared framework with it.

9 MR. DAVERN: And if there was going to be a tax cut, I couldn't argue with that.

10 MR. MILLER: Because with regard to that financial incentive, I think over the longer
11 term, even though there's the one-time cost to the taxpayers associated with it, over the longer
12 term I think you would reap a greater benefit.

13 MR. DAVERN: Well, I guess the thing to do, you know, if there was an agreement to
14 put a mandate on it and then fund it, I guess I couldn't complain, but the problem is we don't
15 have a funding mechanism. But thank you very much for your comments.

16 MR. WANDER: Did you have anything else, Bill, to respond to, Alex?

17 MR. MILLER: Well, I was going to suggest that in terms of being creative in getting
18 the smaller companies over the bar, you may want to look at other approaches, in terms of the
19 SEC being a little more entrepreneurial, might be the way to put it. You could take a page out of
20 what the Commodity Futures Trading Commission did with the Commodity Futures
21 Modernization Act of 2000, which moved away from prescriptive rules to general
22 guidelines, in terms of regulating the industry and the business.

1 There have been a number of other instances in the financial markets taken. Take the
2 derivatives market: there used to be a time when futures had spec position limits, effective
3 position limits or limits on hedgers versus speculators, and they moved away from that. They
4 went to financial responsibility perspective as opposed to arbitrary definitions of what gets you
5 over it. So I think what needs to be done is, there needs to be a creative way of trying to get all
6 firms over the bar, whether it's financial incentives, different types of regulatory approaches, or
7 delegating more to the audit committees, those kind of things, or more to the auditors, external
8 auditors. I think you have to be creative there and encourage firms to grow in the United States.

9 MR. WANDER: For sure. Actually, I give the SEC credit because I think one of the
10 ways they have tried to approach this is by establishing our committee to go out and
11 try to find out, sort of independently from the SEC, ways to creatively deal with these issues. So
12 your suggestions are very helpful, and if you have any other suggestions, particularly in this area
13 which has been very difficult and even, I think, most of the people who are strongly in favor of it
14 have indicated to us that the implementation, at least in the first year, wasn't very good.

15 MR. MILLER: It wasn't a pleasant experience being on the audit committee and
16 meeting as many times as we did for as many hours, I agree.

17 MR. WANDER: So we are still looking, and you have plenty of time to get to us
18 additional suggestions on how to deal with this. Other questions? Bob?

19 MR. ROBOTTI: Actually, this is kind of as much a point of information: You know,
20 the process with small microcap companies in the regulatory process and in recommending 404
21 and the costs associated with that, it's not a new capital-raising issue, most of those companies
22 are not in the process of raising new capital, the vast majority of the shareholders of those
23 companies, you know, will have bought them in the after-market, so that capital really doesn't

1 have a mechanism, it doesn't have a protection to suggest that those companies eliminate off the
2 base, because they don't take it private. They just de-register, therefore, the flow of information
3 is discontinued. You have really disenfranchised all of those investors in those companies. So
4 it's not that they will be raising new money so, therefore, a new investor will have the authority
5 and the power to say, "Listen, this is the information I need; these are the protections I want."
6 Yes, on a new capital-raising situation would be true, but that's the vast minority.

7 So the vast majority are incumbent investors who potentially are really going to be forced
8 out of the process and out of the protections, and include the SEC's mandate is to protect
9 investors, and of course those investors will have no protection because the company will be
10 exempt from filing.

11 So, you know, it's clearly, in my mind, the cost benefit is very substantial, microcap
12 companies which you don't invest in really are a different universe, I do think, and the cost
13 benefit becomes much more significant. There isn't the process where it is raising new capital,
14 so, therefore, the market will take care of itself. Instead, I would argue it's the reverse, let the
15 market take care of itself. We talked about these issues in terms of issues foreign markets and
16 certain investors will invest in foreign markets even though the flow of information is
17 significantly less than what it is in U.S. companies, if they were not filing companies.

18 Let those investors make those decisions, because that's really what we've talked about here.
19 Microcap companies really are a different class of investment. The vast majority of institutional
20 investors who come here say they don't invest in them, so, therefore, there is a higher cost of
21 capital. That is reality.

22 So we are not going to put something on it, make the new universe; that is the universe
23 that exists. And in that universe, to mandate these costs with very little, if any, benefit and not

1 at least let the companies make those determinations --and let investors make those
2 determinations and instead to disenfranchise the investors, which would happen in the
3 deregulation process, that's a huge mistake. So that's why I do think that , even
4 though people say you can't apply it differently, although everybody who said that also said,
5 "Gee, the implementation can be tweaked and has different applicability, because the situation is
6 different." That's our mandate. We really need to make that change, otherwise other investors
7 who don't invest in those small cap companies, the ones we are talking about potentially giving
8 some kind of safeguard to -- they are going to be damaged in the process and there is no benefit
9 being derived. That's a long litany, it isn't a question, but it's informational that follows up on a
10 company board we've talked about who don't invest in microcap market. And a lot of the rules
11 we're talking about potentially changing compliance really is that subsection of the market.

12 MR. MILLER: But the issue that we are wrestling with is even though we are not
13 investing n it, it gets picked up in the general market. To that point, I think we are not talking at
14 each other as much as I think it may appear to be, because it's just a matter of how we segregate
15 it so that the investing public knows that there was a difference, and that that's a consequence of
16 it. But at the same time, I go back to the question raised earlier which is just because you
17 have Sarbanes-Oxley compliance, it doesn't mean you are not going to have restatements. You
18 are not going to have these potentials for fraud, particularly when you have collusion. They're
19 going to happen, I agree with that, and I'm calibrated to, but I would take the view that they will
20 be less than what otherwise would have been the case without SOX.

21 MR. WANDER: Yes, Marty?

22 MR. WHITMAN: Yes, I have two comments.

1 One, in the overall scheme of things, when companies are audited, there is damn little
2 fraud. If you want to take it as a percentage of filing companies, it's relatively rare.
3 Unfortunately, it's more frequent than it was ten years ago, but it is still relatively rare. And you
4 can Sarbanes-Oxley up the "cazoo," but nobody is going to be able to understand GAAP unless
5 they take a balanced approach and read financial statements and footnotes, where they get a lot
6 of disclosure. They don't get accuracy, but if you want to understand the business, God damn it,
7 you'd better sit down and read financial statements. We have done it for 50 years very
8 successfully. We don't need Sarbanes-Oxley. Creditors don't need Sarbanes-Oxley. The only
9 ones who seem to be involved are short-term stock market speculators, that is people who think
10 they are very much influenced by day-to-day price fluctuations, and that isn't most money.

11 MR. MILLER: See, I would counter that with the comment that over the more recent
12 past, I think we have seen a significant increase in the compensation of upper-tier management,
13 and I think that Sarbanes-Oxley serves as a counter balance to such large incentives which could
14 cause actions to occur which may not have happened in the past, as it relates to fraud.

15 MR. WHITMAN: I don't think you can equate compensation with financial statements.
16 The compensation has been increasing in leaps and bounds and there are all sorts of reasons. It's
17 the first time I ever heard GAAP blamed.

18 MR. WANDER: I am not sure Bill is talking about GAAP --

19 MR. MILLER: I am not.

20 MR. WANDER: -- but it might be the incentive systems.

21 MR. MILLER: Exactly. We saw it in the derivatives' world many years ago, as it
22 related to those individuals who were compensated heavily, to take advantage of corporations
23 that didn't fully understand derivatives, Gibson Greeting Cards, Proctor & Gamble.

1 MR. WHITMAN: There has been tremendous, a tremendous increase in compensation
2 to failed managements. Need I say Hewlett-Packard? I mean, if we want to have a meeting
3 about excess compensation to failed managements, we don't have enough time.

4 MR. ROBOTTI: Herb, if I could just follow-up on one point that Marty raised, and
5 that's part of the problem is a company that has the right probably to de-register can accomplish
6 that and in the process the requirement to give audited financial statements is no longer really
7 present. It's not present. It really depends on the state. The state probably doesn't say you have
8 to have properly audited financial statements. So, as an investor in small cap companies,
9 microcap companies, to have an annual audited financial statement, with all of the footnotes, is
10 8,000 times more valuable to me than the fact that it had gone through a 404 audit, which doesn't
11 give me any comfort at all. That's what you are going to end up doing for a significant number
12 of companies. Because we are going to impose a regulation with really no benefit, we are going
13 to subject shareholders to no flow of information and those cost benefits just don't make any
14 sense in my mind.

15 MR. WANDER: Any other comments? Leroy?

16 MR. DENNIS: I just have one comment, Bill, and I haven't read The New York Times'
17 article. I am not up on the Refco, all of the facts, other than what I have read in the papers,
18 but I am troubled by your comment that says apparently this was a fairly successful IPO, and
19 investors didn't care that they had weaknesses -- at least there were enough investors that didn't
20 care, that they had successful IPO. What do you see that we need to do to make it so that they do
21 care? Because I'm almost, why are we bothering with all of this cost if a company can go out
22 and raise a significant amount of capital with material weaknesses? It seems like why
23 bother?

1 MR. MILLER: I can only speculate as well with regard to that, but I have to believe two
2 things: One is, there probably are investors who didn't participate in the IPO because of that, and
3 I can also suggest that this is going to be a learning experience for many people, as it relates to,
4 in the future, not having it is going to require greater scrutiny.

5 MR. WANDER: Judy?

6 MS. VALE: I would just like to make a comment that as sad as it may be, I think,
7 perhaps even a majority of investors do a pitifully small amount of homework, and something
8 which Marty has been harping on, that is that his firm looks at the financial statements is so key
9 to the way someone should invest and do their homework, and a lot of inference is given. But
10 the fact of the matter is that whatever hoops you make companies jump through,
11 you can't assume that people are going to do the minimum due diligence on their part to even
12 read a prospectus. I mean, how many people do you think really read a prospectus from cover
13 to cover?

14 MR. WANDER: The people who write them.

15 MS. VALE: At least the portions that supports --

16 MR. DAVERN: Some of the people that write them.

17 MS. VALE: I mean, it's a very sad fact. And aside from this whole issue of Sarbanes-
18 Oxley and 404, I think that a tiny proportion of analysts on Wall Street, who are supposedly, or,
19 rather, who are experts and who are publishing on companies, even read the financial statements.
20 And there is no way that you can prevent them from making mistakes since they are not doing
21 basic homework now.

22 MR. WANDER: As a securities lawyer I would add, they should also read MD&A,
23 which tells you what the financial statements should have told you --

1 MR. WHITMAN: Great invention, MD&A.

2 MR. WANDER: -- in my opinion. Any other questions or comments?

3 MR. CLOUTIER: Herb, Rusty Cloutier.

4 I wanted to thank Marty. I really enjoyed his testimony, and being a credit lender, I
5 agree with Marty a great deal. When you are loaning money on credit, you do your homework
6 and you don't count on somebody else doing your homework for you. I just thought his
7 testimony really had influence on me today, and I find it very, very interesting that we worried so
8 much about the small investor -- and I agree with the comment that they're not doing any
9 homework, they are being led down the path -- and it is interesting that people that are in it for
10 short-term profits, they'll swing companies, hedge funds particularly and short sellers are the
11 ones screaming and hollering about they don't want any more disclosure, any more regulation,
12 but they certainly don't have a problem putting it on the smallest companies, which can the least
13 afford it. So I thought it was interesting, Marty, you raised some very good ideas today and
14 really helped my thought process, I appreciate it.

15 MR. WANDER: Marty, Rusty is a banker.

16 MS. DOLAN: Herb, this is Janet. I have a question for Judy.

17 MR. WANDER: Go right ahead.

18 MS. DOLAN: In light of your last comment, how are we to reconcile somebody like
19 Bill who comes in and says "Sarbanes-Oxley and 404 everything is well calculated, don't touch a
20 thing," and your comment, which to me suggests that all of this regulatory action is really all
21 about just making people feel good. It's a reaction after every time investors do foolish things,
22 but it doesn't prevent any foolish action by investors in the future. It is just basically to make
23 people feel like the government is doing something, but it never really has any effect on or it

1 doesn't really change investor behavior. This was a very expensive, feel-good
2 action, if that's the situation. How do you reconcile differences between those two?

3 MS. VALE: I don't think that's what I was trying to say. I think it's the responsibility
4 of an organization like the SEC to make certain that companies comply with reasonable
5 regulation to give investors the tools to make intelligent judgments, and this is very important.
6 But I am just being realistic, that you cannot prevent people from investing in ways that may not
7 be wise.

8 I think they are really separate issues, and I think that what you should be focusing on at
9 this point is looking at Sarbanes-Oxley in its various pieces, and do a cost benefit analysis. I
10 thought that was what you were really trying to get at. I think it's reasonable that you are
11 going to have a variety of opinions, depending on how someone invests and how they perceive
12 the costs and the benefits, so I don't think it's so surprising that you have people that are as
13 differing in their viewpoints as the people on this panel, but I think that this is really what you
14 want to focus on. And I think that probably -- like I have been shocked and I've learned
15 something as I am sitting here listening to other people's testimonies today. The idea that a tiny
16 company might be paying percent of their revenues for compliance of something like this, I am
17 thinking to myself, you know, what on earth are they doing? What kind of business is this?
18 How could it possibly cost so much? But if this is indeed the case, this is insane.

19 I think that -- I know that I, for one, do not have the statistics at my fingertips to know the
20 average costs of companies of various sizes, and maybe something that you should be doing and
21 perhaps you already have the information at your fingertips, is finding out exactly what the costs
22 have been, both external costs and imputed internal costs. In other words, hours spent with
23 people already on the payroll, to give you a better handle, at least on the cost side. But I think

1 it's very naive to think that Sarbanes-Oxley is going to prevent fraud. I think everyone in this
2 room agrees that that is not doable, particularly not with this.

3 MR. WANDER: I think we should move on. Gerald has been very patient, and we
4 would like to have his presentation. Is it Gerald or Gerry?

5 MR. WHITE: Gerry. Thank you for inviting me. I submitted a letter about a week ago,
6 I don't know if everybody has had a chance to look at it. It had been my intention to make my
7 remarks very short, but I think what I am going to do is expand them a little bit and try to deal
8 with some of the issue that have come up in the last hour.

9 Let me start by staying that I started in this business, in the investment business, as an
10 analyst. Grace & White was established in 1977. We are an investment adviser. We manage
11 approximately \$800 million dollars and less by design than just where we saw the opportunity,
12 we have gravitated towards smaller companies, which includes micro caps and even an
13 occasional pink-sheet company. So that we are well aware of the issues and how they affect
14 companies of different sizes. I also have, as I point out in my letter, some experience as an
15 educator. I have represented analysts before the SEC, the FASB and various other
16 bodies over the years. I should also add that I also prepare financial statements. We prepare
17 audited financial statements. So I guess I've worn every hat but that of an auditor.

18 The first point I would like to make is that I believe that a public company has certain
19 obligations. You cannot have access to public investors without providing the information that
20 those investors need to make informed investment decisions. I have to say that I don't think
21 there is a material difference between what a long-term stock investor needs and what a creditor
22 needs. I think it's essentially the same thing so I think is not an issue that bears very much
23 discussion. But a public company should comply with the same set of rules regardless of size.

1 And it's an unfortunate fact of life that regulation is more expensive for smaller companies. We
2 are regulated, Grace & White is regulated by the SEC, and I assure you that that process is more
3 painful and more expensive for us than it is for a company or a hundred times our size, but it's a
4 cost that we bear. It's part of the price that we pay for having access to our clientele. And I
5 think it's particularly important that smaller companies meet the same requirements as larger
6 companies because smaller companies are inherently riskier. There is less information in the
7 media, both the broad general media and investment-related media about them than about large
8 companies. They tend to have a lower level of internal accounting expertise than large
9 companies. They rely more on their auditors. So that I think to say that smaller companies
10 should not meet the same hurdles as a large company is a very dangerous and plainly wrong
11 point of view, which essentially brings us to the cost issue, which I think is what this is all about.

12 I think most people agree with the objectives of Sarbanes-Oxley, and the question is why
13 has the cost been so high, particularly for smaller companies? And I think we sort of need to ask
14 a somewhat different set of questions than the ones I've heard earlier today. One question that
15 occurs to me is how have auditors been able to attest to financial statements for companies if the
16 internal controls were not adequate for them to rely on the data that appears in the financial
17 statements?

18 My understanding of Sarbanes-Oxley and Section 404 in particular, was that it was
19 intended to make the process of preparation, issuance of finance statements more reliable,
20 because when I look at financial statements, and parenthetically I should say that's what we do.
21 We never buy anything without having read the financial statements very carefully, and I have
22 written a textbook which purports to tell people how to do that. But the financial statements, as
23 wonderful as they are and as much better as they are than they were 20 years ago, are only as

1 good as the process that generates the numbers. If there are flaws in that process, then investors
2 like myself and the others at this table are trying to make distinctions using fundamentally
3 flawed data. And I think that's what Sarbanes-Oxley was intended to remedy; to make sure that
4 the financial statements had a higher degree of reliability.

5 Unfortunately, I think the response has been to add another layer of audit by check list. I
6 had the dubious privilege a few years ago of being allowed to view the check list that one of the
7 major firms use as part of their audit process. And what I think I learned from looking at that is
8 that they go about auditing not by understanding the company and not by thinking about what are
9 the areas we need to look at to make sure the financial statements are accurate, but they look for,
10 you know, are there leases? Well, if so is there a footnote? The footnote may be wrong, and we
11 discovered that companies of all sizes apparently never read Statement 13 on leasing, but there
12 was a footnote on leasing, so we can check off that box, and so on, down the line.

13 Actually, I understand that the major firms are in the process of preparing a common
14 check list for 404, and I think what the problem is, is that the fundamental audit process is flawed
15 and 404 is just compounding it. If you -- I have met partners of every major accounting firm,
16 and if you meet the partners who are the experts on technical standards, they know everything
17 there is to know about everything, but somehow that doesn't work its way down the line into the
18 audit of individual companies. And I am not sure I can say -- this is something I have said a
19 number of times over the years, that auditors need to think about the company they are auditing,
20 not just do things by rote period, I would argue just as strenuously that analysts and portfolio
21 managers need to read financial statements and understand them. I have said publicly that the
22 only people that invest in Enron, that there are two classes: Those who didn't read the financial
23 statements and those who didn't understand them, because I felt very strongly that there were not

1 flashing red lights but flaming red arrows that would have told anybody who read and
2 understood that this was toxic.

3 So I think, I guess, my closing of my remarks at this point is to suggest that the advisory
4 committee focus on the process: How are 404 audits done? Can the process be done in a way
5 that meets the objectives of the Act? And I would be pleased to answer any questions.

6 MR. WANDER: Very succinctly stated. Thank you very much. Just a minute, Janet.
7 That's been our whole odyssey, I guess, from day one, is how to get there. Interestingly, there is
8 a lot of literature about the accounting profession and audits, et cetera, and frankly that's why, I
9 think, MD&A has taken over so much prominence now is the financial statements themselves
10 don't tell us enough and, therefore, you need sort of to peak underneath the covers to see what is
11 going on. In any event, Janet, enough said by me.

12 MS. DOLAN: First of all, I want to thank you very much for your comments, and I
13 wasn't -- I think you said you submitted written comments, if you did I haven't read them yet, so
14 if the answer to my question is in your written comments, I apologize. But I think Herb has kind
15 of hit nail on the head. We are all trying to, I think, achieve what you are suggesting, which is
16 how can we get to the point where these audits, particularly 404, how can we get these where
17 they are more company-specific, where there's more rational judgment brought to bear on how
18 do you actually do a good 404 for this particular company and not have a one-size-fits-all
19 approach, but how do we get there?

20 You, I presume, read the PCAOB May 16th proclamation that tried to bring more of a
21 rational approach to this, but we have had testimony that audit firms don't think they will change
22 their behavior as a result from it. Do you have some suggestions of how we get there? You are
23 very knowledgeable in this area. What specifically could either the SEC, the PCAOB, or us do

1 to help us get to that point where this is a better, a more rational approach in the implementation
2 process?

3 MR. WHITE: I wish I had a good answer to that. I think it's an educational process
4 within the auditing community that's mainly -- that's mainly needed. I have to say the market
5 does seem to be -- the market does seem to be moving a certain way in that smaller firms seem to
6 be clearly gravitating away from the largest auditors to smaller auditors. And I suspect that not
7 just audit costs, but 404 costs are driving that process. And my impression is that the smaller
8 firms at least feel they are able to do what is necessary at lower cost. It may be that because they
9 are smaller, there is less of a disconnect between the knowledge at the top of the firm and what
10 happens down the line at the individual company level, and that may be the answer. I think
11 when I started this business a company that went public was told, "You have to have a big 8
12 accounting firm." I haven't heard anybody suggest that in years. I think that's part of the answer.
13 I don't see any evidence that the large firms do any better job than the small ones.

14 MS. DOLAN: Do you think there is any specific guidance or any specific clarity that the
15 PCAOB or the SEC should be issuing to give more latitude to the audit firms or more power to
16 the audit committees or something? Is there anything within the regulatory framework that you
17 think could advance this significantly?

18 MR. WHITE: I am getting out of my area of expertise, but I would say that trying to
19 establish guidelines or what is the purpose of the process and trying to get everybody to
20 understand that so they do what is necessary to make the financial statements reasonably correct,
21 without going way beyond into auditing numbers for the sake of numbers. I promised myself
22 before I started that I wouldn't tell war stories, but I will tell you one. I have a client who is
23 accountant is meticulous, endlessly meticulous, to the point where he will spend hours of his

1 expensive time working out something that is worth far less than his time is worth. And that's
2 just how he is and the client accepts it and it is not -- I am not the one to complain about it. But I
3 think there can be, I suspect there is some of that in this person's approach.

4 MR. WANDER: Jim?

5 MR. THYEN: Yes. Two questions for the panel: We have talked about investors should
6 make informed decisions; we have talked about the value of doing the homework and the value
7 of the tools that come out of the regulated markets and were ready to comply with regulations,
8 including 404. Should investors that do not do their homework, do not use the tools, do not
9 focus on understanding the financials, should they have the same access to recourse and redress?
10 I would appreciate hearing your views and opinions.

11 MR. WHITE: I am not here to defend the plaintiffs' bar if that's where the question is
12 going. I mean, let me answer your question this way: I view the financial reporting systems as a
13 database that investors are free to use and those that use it use it in different ways. I mean, Marty
14 Whitman and I, if you were to hear us describe our investment process, it sounds the same. If
15 you would look at our portfolios, you will see a little bit of overlap, but very little. And that's
16 true of every value investor that I know of, the overlap is incredibly small, because we all do it
17 our own way. But the database serves everybody and needs to be broad enough to serve
18 everybody's needs. Now, what do you do about somebody who chooses not to use it and then
19 files suit about it? As I said, I am not here to defend the plaintiff's bar.

20 MR. THYEN: There's the example of Enron investors.

21 MR. WHITMAN: Well, one, to get where I am coming from, I, of course, think that
22 Sarbanes-Oxley ought to be repealed in its entirety because it doesn't help the serious investor. It
23 doesn't help either the investor or creditor for whom you ought to be providing disclosure.

1 As far as that's concerned, once things are disclosed, I think somebody who chooses not to
2 use it, you choose not to use it, you suffer the consequence. I don't think the plaintiffs' bar gets
3 very far in lawsuits when things are disclosed. Again, I reiterate, one of the reasons we don't
4 need Sarbanes-Oxley is because you folks and the accounting profession have done such a
5 wonderful job in now providing disclosure in the last years. That's including the MD&A and
6 improvements in the MD&A. I include those with the financial statements.

7 In terms of Sarbanes-Oxley, just to set the record straight, as far as issuers are concerned,
8 it is not only a subject of cost but it's also a subject of potential liability. That's a real issue and
9 to burden these people with both cost and liability without offsetting benefits to serious
10 investors, I have great doubts. Now one of the other things I would like to say, as someone who
11 is very active on a very large company's audit committee, the auditors, especially the big 4, are in
12 a cover-your-ass mode, and they will look hard. When in doubt, say there is a material weakness
13 or material deficiency, it has to be disclosed. I mean, it's very arguable now in this environment,
14 in terms of Sarbanes-Oxley, with participants. It seems to me, from my limited knowledge of
15 bending over backwards to find problems when really no problems may exist in things like
16 internal control, I am not on enough board committees to generalize, in ours it is certainly that
17 way.

18 MR. THYEN: Thank you.

19 MR. WHITE: Can I disagree with, I would like to take issue about the statement about
20 the lack of benefit, and I guess I will use an illustration. Earlier this year I met with the CFO and
21 CEO of a public company which had just restated their inventories. And naturally I asked them
22 about that, and the CEO told me -- this was a new CFO who had been hired the year before. He
23 said the first thing he did as a new CFO was ask him to look at their inventories, because he

1 wasn't -- the CEO was not comfortable that they were really accounting properly for their
2 inventories. And the result was a restatement. When they went through the SOX 404
3 process, inventory accounting was listed as material deficiency, they have now fixed the
4 problem, and it had no negative effect, by the way. I think they were very up front about it, but
5 here is a case where if they hadn't been proactive, 404 would have picked it up. It would have
6 forced the restatement, they acted in advance.

7 MR. WHITMAN: Charles, I think the question is how frequent does that occur? I
8 mean, I don't deny that there is fraud. I don't deny that there are bad audits. It's just that it hasn't
9 been that much of a problem, I see, for neither Judy or myself, and I suspect for most serious
10 investors that's true.

11 MR. DENNIS: The question I would have to follow up with you is what drove the
12 discovery of the material weakness? Was it the restatement? My understanding is most of the
13 material weaknesses have been driven by audit procedures, not by 404 testing, or did the 404
14 testing drive the restatement? Which came first, the chicken or the egg?

15 MR. WHITE: The restatement came first.

16 MR. DENNIS: My understanding is that's fairly typical, is that most internal control
17 deficiencies reported have been as a result of audit, financial statement audit findings that have
18 been -- that we made a material adjustment to the financial statements; therefore, we must have a
19 material weakness in inventory, and it's not the testing that has said, "by doing this testing we
20 have discovered a material weakness that then uncovered a financial statement or reporting
21 problem".

22 MR. WHITE: That is somewhat unknowable, because once the company has identified
23 the problem, it is hard to say whether the 404 testing would have turned it up or not.

1 MR. WANDER: It I could, Jim, one interesting thing is the statistics we have, which I
2 think are not a long enough period to really be valid. The statistics we have are that -- there
3 are like 30, 35, 40 material weaknesses. And they don't clump in any particular area for any
4 particular size company, they go all over the lot. And it's, it was surprising to me and, in fact, the
5 people at the SEC office of economic analysis, that you could not really pick out a pattern based
6 on size of the company and or the particular material weakness. Now that's just based on the
7 first year. Jim?

8 MR. THYEN: A question of a completely different color or different area: We would
9 like to know your opinion on analyst coverage for fees? Do you have an opinion?

10 MS. VALE: Could you be a little more clear?

11 MR. THYEN: Well, when you look to, again, to the smaller public companies and you
12 look at the changes in scope and in make up of analysts and what companies they cover, I was
13 wondering if you have an opinion on the idea of the debate discussion of analyst coverage of
14 smaller companies for a fee?

15 MR. WANDER: Do you mind?

16 MR. THYEN: Sure, go right ahead.

17 MR. WANDER: We had, you know, NASDAQ has partnered with Reuters to start a
18 new system to provide analyst coverage for companies who want to buy it, who don't have it.
19 And the theory is the company would sign up for a three-year period. This NASDAQ subsidiary
20 would then pick three analysts for that company, and they had to agree to do this for, I think it's
21 three years, based on their present analysis.

22 The question is: It's issuer paid for analysis, analyst reports, which has to be disclosed
23 under, I think it's Section of the ' Act, but there is -- we have had a debate whether there should

1 be any company-sponsored analyst reports or whether this system or a system similar to this
2 would have merit. And the feeling is that the analyst community has gone down, the whole
3 business model has not worked recently. So I guess that's Jim's question, not a question.

4 MR. THYEN: No, but it fits in in capital formation.

5 MR. WHITMAN: Jim, I really can't answer, but in terms of standards, I would say
6 anything that informs investors is to the good, subject only to things shouldn't be done that
7 might compromise a free, fair and an orderly markets. You know, I think you are back at the
8 beginning. We rely, I mean for us, I don't know about Judy, but we rely, in domestic investing,
9 almost strictly on SEC disclosure, company disclosure, like annual reports and stockholder
10 quarterlies and meetings with companies. Period. I think a lot of people like me pretty much
11 follow the same routine.

12 MS. VALE: I have a couple of comments and it may not answer your question, but
13 similar to Marty, in my investment group we almost don't use Street research. We use very, very
14 little of it because they simply don't do things the way we do, and we do our own analysis,
15 heavily based on financial statements, heavily based on our own trying to understand business
16 models, competitive pressures within an industry. I don't think that there is a problem
17 with -- I presume you are talking about possible conflicts of interest if a company is paying to
18 have research done about it, if it's fully disclosed. I kind of doubt the utility of it, but then, again,
19 I think a lot of published research now is not too dissimilar in that many Wall Street analysts will
20 describe a business largely in terms of the company's annual report, and in their analysis will
21 largely repeat what management has told them about their prospects, you know.

22 MR. THYEN: Okay.

1 MS. VALE: But I don't think that it would be a problem, I am just not sure what the
2 general utility would be. I almost wonder if it might be, given the fact that Internet is so
3 prevalent now, whether it would make sense to, in a sense, have an investor site under the
4 auspices of the SEC, where anyone can access it on the Internet and any public company is
5 welcome to post whatever they want under their ticker symbol, and they are invited, it's
6 absolutely clear that all of this is tread at your own risk. All of this is coming from
7 companies, how they choose to present themselves. But I don't think it will be substantially
8 different from what you are getting from a paid analyst who, because of the financials involved,
9 is probably going to do something fairly non-critical.

10 MR. WANDER: Thank you. Bill?

11 MR. MILLER: I would be receptive to the model if that's what the micro-cap, and
12 small cap companies wanted to do that didn't have any analyst coverage. I mean, as long as they
13 put the money in and it was such that it was a three-year commitment, it's in, it's in for three
14 years, they paid for three years, the conflict is diminished and whatever comes out of the analyst
15 coverage comes out of it, and I think that would be possible.

16 MR. THYEN: Thank you. Herb, that's all I have.

17 MR. WANDER: Yes, Bob?

18 MR. ROBOTTI: Sorry, I am going to jump back to Gerry and ask him a couple of
19 questions. Obviously you must own stocks in your portfolio that are not accelerated filers and,
20 therefore, not 404 compliant and won't be for an extended period of time?

21 MR. WHITE: Yes.

22 MR. ROBOTTI: Do you have different return hurdles or expectations for those
23 companies? Because I know I own those companies and I feel comfortable the non-accelerated

1 filers and the accelerated filers, and most of those companies may have banking relationships
2 and those bankers may lead their money and the banking environment is also comfortable with
3 lending them money or not, whether or not they are 404 complaint. So I am saying, where is the
4 benefit if we as investors -- or do you view it differently than non-accelerated filers from the
5 accelerated filers?

6 MR. WHITE: We certainly invest in companies with different risk characteristics. And
7 the investments we make -- first of all, we have clients with different acceptable risk levels, so
8 we may buy something that is riskier for one set of clients and not another. I think it's also fair to
9 say that when we view something as higher risk for any reason, we expect a higher return to
10 justify that. We do look at things -- we are not terribly quantitative about it, I have to say,
11 because these things are so hard to quantify, but in general terms, we do look at the risk and
12 whether they have had to meet 404 yet or not, it's hard to separate that out, because we look very
13 closely at financial statements. We prefer -- in fact, if a company is way out there in terms of
14 aggressive accounting, we never get to the valuation question, it goes right out the window.

15 And I might add, because this is something that came up earlier as far as foreign issuers
16 are concerned, we sort of take the same approach. I know enough about non-U.S. gaps to be
17 able to look at non-U.S. companies, but there are risk factors there. The audit environment is
18 different in many countries, and we expect a higher return where we are taking risks that are
19 greater than for a comparable U.S. company.

20 MR. ROBOTTI: But, of course, my question really is: Have you incorporated in a
21 different valuation metric for non-accelerated filers or at this point this is not a concern?
22 Because part of my concern is not so much a concern of the audit environment generally, of

1 course it's becoming more strict and more stringent, so I don't need 404 because the auditors I
2 know are doing a better job of looking into the numbers. So I don't need that extra protection.

3 MR. WHITE: Well, better job some of the time. Yes. To answer your question we
4 have not explicitly made the allowance for that, but smaller companies are inherently riskier so
5 the ones that have not gone through 404, in a sense, there is probably still a demand in premium
6 for that.

7 MR. WHITMAN: Bob, very interesting. About something over 40 percent of our
8 common-stock portfolios are in companies domiciled in Japan, Hong Kong, South Korea,
9 Sweden, Switzerland, all published in English, all audited. It's clear in my mind that if pricing
10 were close to equal, we would so much prefer companies that agree to service the
11 U.S. and agree to comply with SEC requirements.

12 I mean, certainly in general, in your question, if you can get close to equal investments in
13 companies subject to U.S. jurisdiction, if you were I, you would do the U.S. jurisdiction rather
14 than what we are doing now, and doing it in a big way.

15 MR. WANDER: It's a little after 5:00 p.m. Anybody for a final question?

16 MR. CLOUTIER: If you don't mind, Herb, I would like to just follow-up on that
17 question, it was a very interesting question. The question was mentioned again about
18 credit. I mean, on a credit decision we take the financial statements, go to the footnotes right
19 away. I just kind of want to know if this is the way you all would look at it -- and go to the
20 footnotes; we, of course, go back to cash, because that's the most important thing. We convert
21 everything back to a cash basis to determine cash flow, because that's how we get paid and that's
22 where the money really comes from.

1 You know, we kind of take the Warren Buffet philosophy of credit lending, if we can't
2 really understand it, we don't put any money into it. If we can't understand it, if we don't feel
3 comfortable with it at the end of the day, we won't loan them any money. Would not most
4 investment places that put all their sums of money into companies do that kind of --do the same
5 thing; Break down the footnotes, bring it back to a cash basis, which we understand what they
6 have gotten. If they don't feel comfortable with it, move on, since there's like 8000, public
7 companies out there.

8 MR. WANDER: Any takes?

9 MR. WHITMAN: Yes. I'd say our investment style is in no way we are ever going to
10 buy common stock unless a company is extremely well capitalized. If it is not extremely well
11 capitalized, the only thing we ever want to be is the well coveted creditor. That comes first in
12 what we do. But to answer your question, we don't do any common stocks unless we think the
13 company has a super strong financial position. That comes before anything else.

14 MR. BOCHNER: Herb, do we have time for one more question. If not, I won't ask it,
15 but if we do, I would --

16 MR. WANDER: I know your questions are always right to point, so...

17 MR. BOCHNER: I want to ask Gerry and Bobby or Marty to chime in. I don't want to
18 let this opportunity go by without asking their views on the materiality question that we have
19 been struggling with. We have gotten a few comments that SAB 99 is difficult to apply between
20 issuers and auditors, and they are referring a lot of those questions to their lawyers to figure out.
21 This is in the financial restatement context, not for purposes of MD&A or anything else. Does
22 the current regime work well enough and it is just a matter of issuers and auditors working better

1 together and figuring out when an error should trigger a restatement, or should we have more
2 objective standards? I would be interested if you have any views on that.

3 MR. WHITE: I will start because I have some background. The FASB had a task force
4 on materiality -- don't ask me how many years ago. I was a member of that task force, and after
5 a couple of years they disbanded it because the feeling was that it was impossible to have
6 quantitative materiality thresholds. I know there are some formal and informal ones that exist,
7 but our view was -- and that's my view. The materiality is ultimately what would make a
8 difference to an investor? And materiality thresholds are clearly lower for smaller
9 companies, not only in dollar amounts, but I think relatively speaking, because smaller
10 companies tend to have, even well capitalized ones, tend to have less financial flexibility, less
11 room for error. So that for a company that is 100th the size of another, the materiality threshold
12 might be, relatively speaking, much higher, but it's also the nature of the item. If the restatement
13 is because the CEO was stealing, I would suggest even \$10 is material.

14 MR. WANDER: Which is SAB 99.

15 MR. BOCHNER: The thinking, just to expand on that, the thinking is that these days, if
16 you miss by a penny, the stock gets hit. So, yes, that's material. So the argument would be that
17 even little tiny changes now, we would go to the reasonable investor test for restatement
18 purposes, make everybody conservative and go. You know, a penny off, somebody might think
19 that's important, restate. So the inquiry would be whether it should be more objective, just in the
20 context of financial statements. So that you could assume a situation where we don't meet a
21 threshold, so no restatement is required, but you are on your own as to whether you need to
22 disclose it in MD&A or put out a press release, that's a different issue. So that would be the
23 context. That's what we have been wrestling with on the disclosure subcommittee.

1 MR. WHITE: I just don't think that objective criteria are possible, in all honesty.

2 MR. WANDER: It's the Chinese proverb: You might not like what you get. At least
3 that's my view.

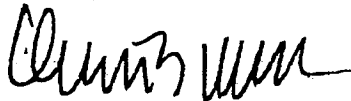
4 In any event, I want to thank our panelists. I don't see any of our first panelists,
5 but this was a little awkward in the fact that you had to answer questions from a loudspeaker, and
6 we greatly appreciate you doing that. Most of our other hearings, we have had everybody
7 present, but this was something that we wanted to finish up. So I want to thank you not
8 only for the sort of awkwardness of this, I think it's actually worked out very well. You have all
9 been very candid, very thoughtful and extremely helpful, and we all appreciate it. Thank you.
10 Is there any other business? If not we can turn off the microphones and web page.

11 Thank you.

12
13 (Time noted: 5:10 p.m.)

CERTIFICATION

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



Herbert S. Wander
Committee Co-Chair

11/16/05

Date

Index of Written Statements Received

Listed below are the written statements received by the Advisory Committee between its meetings of September 19, 2005 and October 14, 2005 and the dates of receipt.

Oct. 12, 2005 Brad Smith; Peter Chepucavage; Stephen Boyko; Frank McAuliffe; Steve Brock, CEO, Public Company Management Corporation; International Association of Small Broker Dealers and Advisors

Oct. 07, 2005 Tony Ryals

Oct. 07, 2005 Martin Whitman and Martin Shubik

Oct. 07, 2005 Jim Carnes

Oct. 07, 2005 Michael V. Williams

Oct. 07, 2005 Jim Miller

Oct. 07, 2005 Don Develder

Oct. 07, 2005 David Patch

Oct. 07, 2005 Philip V. Oppenheimer

Oct. 07, 2005 Jay Bee, Columbus, Ohio

Oct. 07, 2005 Gordon W. Bader

Oct. 07, 2005 Thomas A. Russo, Partner, Gardner Russo & Gardner

Oct. 06, 2005 Gerald White, President, Grace & White, Inc.

Oct. 05, 2005 Brian Furrer

Oct. 05, 2005 Francis X. Milano, President, Strategic Investor Relations Corp.

Oct. 04, 2005 Philip Bursley, El Paso, Tx.

Oct. 04, 2005 Gilbert M. Erskine

Oct. 04, 2005 Mary Helburn

Oct. 04, 2005 Henry Elz

Oct. 04, 2005 Donald B. Miller

Oct. 04, 2005 Ralph Gang

Oct. 04, 2005 Mhat McCane

Oct. 04, 2005 Jim Leary

Oct. 04, 2005 Glen Kelly, Investor/Shareholder

Oct. 04, 2005 George Bingham

Oct. 04, 2005 Robin Lisk

Oct. 04, 2005 Larry C. Gadbois

Oct. 04, 2005 Philip Robinson

Oct. 04, 2005 Tom Vallarino

Oct. 04, 2005 Robert W. York, Individual Investor

Oct. 04, 2005 Christopher Rice

Oct. 03, 2005 Thomas M. Sullivan, Chief Counsel, and Michael R. See, Assistant Chief Counsel, U.S. Small Business Administration Office of Advocacy

Sep. 19, 2005 Larry E. Rittenberg, Chair, Committee of Sponsoring Organizations of the Treadway Commission
