RECORD OF PROCEEDINGS OF

SEC ADVISORY COMMITTEE

ON IMPROVEMENTS TO FINANCIAL REPORTING

OPEN MEETING

Thursday, August 2, 2007

10:00 a.m.

SEC Headquarters

100 F Street, N.E.

Auditorium L-002

Washington, D.C.

COMMITTEE MEMBERS PRESENT

Dennis Beresford
Susan Bies
Michael Cook
Jeffrey Diermeier
Scott Evans
Linda Griggs
Joseph Grundfest
Gregory Jonas
Christopher Liddell
William Mann, III
G. Edward McClammy
Edward Nusbaum
Robert Pozen, Committee Chair
James Quigley
David Sidwell
Thomas Weatherford

COMMITTEE MEMBERS ABSENT

Peter Wallison

OFFICIAL OBSERVERS PRESENT

Robert Herz
Kristen Jaconi
Arthur Leder for Charles Holm
Mark Olson

OFFICIAL OBSERVERS ABSENT

Phil Laskaway

SEC AND COMMITTEE STAFF

Conrad Hewitt, SEC Chief Accountant
Jim Kroeker, SEC Deputy Chief Accountant
John White, SEC Director of Division of Corporate Finance
Russell Golden, FASB Senior Advisor to Committee Chairman

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P R O C E E D I N G S

(10:10 a.m.)

OPENING REMARKS

CHAIRMAN COX: Good morning and welcome to the Securities and Exchange Commission. I am pleased to be here for this first meeting of the advisory committee on improvements to financial reporting, and I want to welcome all of the members of this committee and thank each of the members and the observers for agreeing to serve. I particularly want to thank the committee's chairman Bob Pozen for his leadership.

Earlier this week we celebrated the fifth anniversary of the Sarbanes-Oxley Act. The stated purpose of that act was to "protect investors by improving the accuracy and reliability of corporate disclosures." Among its many provisions the act rather presciently called for an examination of ways to combat growing complexity in financial reporting.

If you remember that in one of the paradigm cases that led to this landmark legislation, the Enron case, much of the fraud was hidden in a thicket of accounting complexity.

The act called for studies on the use of principles-based accounting systems and disclosures regarding off balance sheet transactions. These resulted in well thought out reports to Congress on ways that financial reporting could be improved. Many of those reports have recommendations that have already been implemented or that are in the process of being implemented, but this work and these reports were just the beginning.

We've continued our efforts by joining with the FASB and with the PCAOB in an all out war on complexity in accounting. When it comes to giving investors the protection that they need, information is the single most powerful and important tool that we have. And surely we can't say that we have achieved our investor protection objectives, not only the mission of this agency but the very stated purpose of the Sarbanes-Oxley Act, if the information is provided in a way that isn't clearly understandable to the men and women who use it to make decisions.

The truth is that financial reporting has become overly complex. That means not only are financial statements difficult for investors to understand but also companies incur excessive cost as a result of complying with voluminous and overly prescriptive accounting and reporting rules. Your job on this committee is to help us end this destructive cycle and to get our financial reporting system back to first principles.

We're asking you to help us reduce complexity and all of its costly burdens. When it comes to financial statements, most investors today would probably find themselves agreeing with Mark Twain who said, "the more you explain it, the more I don't understand it." That's why we've called on leaders from the private sector to advise us on what steps we need to take.

Empowering investors doesn't just mean better access to information. It also means access to information in a form that they can really use. So simply put the question is, once that SEC-mandated information is available, is it useful, is it understandable? And the answer, all too often, has been a resounding and frustrated "no," particularly among individual investors at a time when over half of U.S. households own securities.

It's even more frustrating when the process of preparing that information by issuers involves unnecessary costs and procedures and uncertainty about what is required of them. That's why I am so pleased to have chartered this committee.

The Committee on Improvements to Financial Reporting already has a catchy acronym, CIFiR, which brings to mind the cryptographic tools of the intelligence community. Well, it shouldn't require a secret decoder ring to understand what's going on in your financial statements.

So with your help today we are opening up another front in our war on complexity by gathering the views of a wide variety of constituents including preparers and users and those who assist and advise them. We look forward to this committee providing specific recommendations on how unnecessary complexity in the financial reporting system can be reduced and how the system can be made more useful to investors.

Your enabling charter describes several areas that the committee will focus on, including the current approach to setting financial accounting reporting standards, the current process of regulating compliance with those standards, factors that may drive unnecessary complexity and reduce transparency, and any lessons that can be learned from the growing use of international financial reporting standards.

I've also asked the committee as part of its consideration of our financial reporting system to focus on how technology might be used to address accounting complexity by making financial information more useful to a greater number of investors. For example, through the power of interactive data the opportunity exists to redesign the financial reporting system to deliver precisely the type and level of information that each individual investor needs.

I want to thank the members and observers once again for your participation on this advisory committee. I look forward to your work, as do my fellow commissioners, and your thoughtful recommendations on this vitally important mandate.

I want now to turn it over to our Chief Accountant, Conrad Hewitt, for his introductory remarks.

ADDITIONAL INTRODUCTORY REMARKS

MR. HEWITT: Thank you, Chairman Cox and good morning to everyone. Also I'd like to welcome all of the committee members to the first meeting of the Advisory Committee on Improvements to Financial Reporting.

The formation of this committee has been a top priority for me. When I first interviewed with Chairman Cox over a year ago, becoming the Chief Accountant, he indicated his desire to form a committee to study how we could make improvements to our financial reporting system.

As part of this effort he wanted to see what could be done to reduce the complexity of financial reporting for the benefit of companies and investors. Based upon my experience on several boards and as chairman of several audit committees, I too thought this was a worthwhile endeavor and its one of the main reasons I am here.

I'm very happy to be able to address the committee and welcome it to the public.

Now the U.S. system of financial reporting has long been the most robust and transparent in the world. However in order for us to retain our position as the gold standard we must from time to time step back and evaluate what changes may be necessary.

From my various roles as an auditor, director of a board, audit committee chairman and regulator over the years, it has become increasingly apparent to me that the current system has become overly complex. The financial reporting system needs to be improved to more effectively meet the needs of the entire spectrum of investors.

As you know, the Commission's mission is to protect investors, maintain fair, orderly and efficient markets and facilitate capital formation. Financial reporting permeates every aspect of this mission, making this committee an important element in supporting the Commission's role in the U.S. capital market.

Please consider the following. As Chairman Cox just mentioned, today equity securities are broadly held with approximately half of the American households investing in stocks. This presents a challenge. Investors have expressed concern that one-size-fits-all financial reports of today do not meet the needs of the spectrum of investors that rely on these reports.

Individual investors may be interested primarily in summarized, plain-English reports that are easily understandable, and may find it difficult to understand all of the underlying detail, including the financial reports that are currently produced.

On the other hand, market analysts and other investment professionals may desire information at a far more granular level than is currently provided. Technology certainly must play a future role in delivering the customized level of information that different types of investors may desire and need.

Aside from the investors' concerns companies have expressed concerns with our current financial reporting system. Many companies assert that it's difficult to ensure compliance with the voluminous requirements contained in U.S. GAAP and SEC reporting rules when preparing financial reports.

In fact, during 2006, this past year, almost 10 percent of the U.S. public companies restated their prior financial reports. To me this is an alarmingly high number and really has the potential to obscure those companies with serious underlying problems as opposed to those companies with unintentional misapplications of complex and nuanced accounting literature.

Restatements are costly to companies and can undermine the confidence of investors in our financial reporting system. So committee members, as you study these issues I encourage you to look beyond the accounting applied in the basic financial statements and footnotes. I believe you should consider more broadly the array of information that investors need to make informed decisions.

Today the U.S. capital markets can run fairly orderly and efficiently, but only through the steady flow of comprehensive and meaningful information. As some have noted, the percentage of a company's market value that could be attributable to accounting book value has declined significantly from the days of a brick and mortar economy.

Thus, you as a committee may want to consider a more comprehensive business reporting model including both financial and nonfinancial key performance indicators. I think we all must also consider how to deliver all this information more timely.

In the twenty-first century, in a world where messages can be sent across the world in the blink of an eye, it is ironic that the analysis of financial information is still subject to many manual processes resulting in delays, increased costs and errors.

Now as you can see the improvement of financial reporting involves more than -- for example, an effort to trim down hundreds of pages of guidance on accounting for derivative instruments. Instead, to me, improvements to our financial reporting goes beyond the complexity debate to encompass the usefulness of financial reporting and the delivery of information to investors.

As you consider these issues I encourage you also to consider how you would define complexity and the scope of areas that you believe should be addressed as part of an effort to improve financial reporting. Throughout the next year I encourage you to consider the expertise and work performed by others in tackling the many facets of this issue.

Academics, organizations and private citizens alike have performed research and provided numerous recommendations that may bear on the matters you will deliberate. They will also continue to do so via the many opportunities for public comment that you as a committee will provide.

Now in some cases activities related to the many topics you will consider are already underway. For example, reconsideration of the conceptual framework by FASB and IASB, codification of U.S. GAAP by FASB, international convergence efforts, development of an enhanced business reporting framework and use of XBRL among others.

However I also encourage you to begin your considerations with a blank sheet of paper, an open mind that is not bound by past precedent, current activities, popular or fad views, opinions or political pressure. I suggest that maybe you want to think outside the box.

Now I recognize the ambitious nature of our goals and the enormous amount of work ahead of us. However with the formation of this committee we have the potential to continue to improve our financial reporting system, solidifying the position of U.S. capital markets as the most transparent and reliable in the world.

I am confident that with your varied backgrounds, experience and points of views as well as the participation of those that you represent in this process we will be able to address the matters that lie before us.

In closing, for many years into the future investors should benefit from your recommendations. I sincerely appreciate your commitment to this committee. My staff and I look forward to working with you in this process and I personally thank you for joining this important committee.

With that, I'll turn the floor over to my deputy chief accountant Jim Kroeker who will call the meeting to order, and then he'll turn it over to the chairman, Bob Pozen.

Jim. Thank you, all.

MR. KROEKER: Thanks, Conrad.

I just wanted to echo the thanks that Conrad and Chairman Cox have already expressed to the committee members. Considering how to improve the usefulness of financial reporting is an extremely important endeavor and one that I and our staff look forward to working with the committee on.

In the interest of hearing directly from committee members on the discussion of the content of this meeting I won't make any additional remarks. Rather, I'll turn the floor over to the committee chair Bob Pozen.

Bob, the floor and the meeting is yours.

MR. POZEN: Thank you, and thank you, Con, for those excellent remarks. I'll just sit here in order to generate the committee quality of discussion that we hope to have this morning. I'll just make a few preliminary remarks and then move us into the discussion paper.

I would say that the reason why we need -- why do we need this committee? In my mind, there are three main reasons. One is, if we look at this from the preparers' and the auditors' point of view, those are the people who put together financial statements. As Con pointed out, we in 2006 had about 10 percent of all U.S. companies that restated their financials.

This is a group of people who are trying very hard to get it right. They have a lot at stake in getting it right, yet we have this very, very high volume of financial restatements. So that shows that we aren't really giving enough guidance to people. We don't have these standards right.

When that many people try that hard and have that high an error rate it's not a good result. The second thing is that we look at users. We see individual investors. Many individual investors tell us that when we get these 10-Ks or prospectuses they just can't read them, they put them in the trash. That's not a very good place for disclosure documents.

They want summaries. They want easy. They want something that they can grasp quickly.

On the other hand, if you talk to sophisticated investors they'll tell you that there's not enough information, and it's not in the right format, it doesn't go deep enough, there aren't enough indicators. So we have two groups that -- one of whom wants a much simpler format and another which wants a much more sophisticated format. We've been a one-size fits all and it doesn't seem to fit that well.

The third thing is the growth of press releases. For those of us on audit committees or companies it's like the press release has become the alternative communication vehicle. This is a vehicle which summarizes what the company has done in the last quarter of the last year and it also contains a lot of non-GAAP financials, which are the company's way of saying, "look, this is what's really important; these are our core earnings; let's strip out things like currency fluctuations," or things like that.

So I think these are three things that really indicate that we have a problem. We have a very good system but we really need improvement. It's not so easy to solve these problems, or as we're going to say to decipher these problems. We have various pundits who say, well, what we need to do is just adopt the UK system of principles versus rules or the IFRS system of principles.

I think we all understand that in any of these systems they have rules as well as principles and the real question is how do you mix principles and rules. And I think it's also true in the U.S. litigation environment there is a desire for rules to protect people who are in good faith trying to get the system right.

So I think we can make some headway in that, but I don't believe that the principle versus rule distinction is the solution here. It's an aspect that we can look at, but we shouldn't believe that that's the answer.

The other thing that we have to recognize is some of the reason that we have complexity is because the economic transactions are complex. Some of the reasons we have complexity is because we have a difference of viewpoints between preparers and users. Most sophisticated users, for instance, would want more segments, but preparers don't want to have as many segments.

So these are very real and genuine tensions in the system and they are not easily resolved. But nevertheless this committee will come to grips with these issues in, I believe, a very deep and fundamental way, and we are committed to coming out with proposals by next August.

And I would say the proposals I hope will have two characteristics. One is that they'll be doable; that is, they'll be easy to adopt. That first of all means that they will not require legislation. We should try to stay away from proposals that require legislation because Congress -- once things get into Congress it's a very difficult environment in order to implement something.

The second thing is that we do have the support of the SEC, FASB and PCAOB and we ought to take advantage of that. There have been many commissions in the last few years by different private groups, but those are commissions that have just basically decided they want to put forth their view to the agencies. Here the agencies have said we need help, we want your input and we are happy to have -- Con, your support, Bob Herz's support, Mark Olson's support and various staff members like Jim and Russ who will work with us.

So this is not a case in which we're going to come out of the blue with these proposals next August. We're going to have vetted them. We're going to have worked with people so that these will be, in my view, doable. The other thing is I would hope that the proposals would be focused. Focus, focus and focus as they say in real estate.

We cannot possibly address every single issue in financial reporting. This is a huge subject and there are many areas, many aspects of it, but we can focus on those areas where we think we can make substantial improvements. We want to identify those areas where there's a consensus that there is something wrong and we can improve it by doing various things.

And I think if we can focus on those areas and identify those areas that that will be a success. So this committee should not be judged at the end by whether we have 100 recommendations. I hope we won't have 100 recommendations. I'd rather see us have 10 or 12 recommendations of things that are actually doable which really substantially increase performance.

Now I'd like to turn to the discussion paper. This is in the booklet that has been handed out to you with a very nice cover. And I should say that this represents my view and not the views of the Commission and it actually doesn't even represent the views of the committee because they hadn't seen it until a week or two ago.

But this discussion paper attempts to lay out five areas where the committee may choose to focus, and within that to delineate issues that could be addressed. The five main areas are substantive complexity, the standard setting process, number two, compliance audit, number three, delivery of information, number four, and international coordination, number five.

Just to sort of help the group here in the audience, by substantive complexity we mean some of the things that Chairman Cox is talking about, why are these accounting standards so long, why are people having difficulty following them, difficulty comparing them, why are they so complex? In the standard setting process we're talking about how the FASB goes about adopting accounting standards and probably more importantly how they get interpreted down the line as people come to actually apply these standards either at the registrant level or at the industry level.

In the compliance audit area we're talking about how the audit process occurs, what happens between accountants and their companies and we're talking about how these financial statements are reviewed by Corp Fin here at the SEC and ultimately the inspection process at the PCAOB, the inspection process of auditors and the enforcement process at the SEC.

The fourth area we're looking at is information delivery. This is an area where we're talking about how we can take the body of information and deliver it to investors in formats and packages that are more appropriate to their needs. How can we go to summary prospectuses, how can we use some of the things that Chairman Cox is doing in XBRL to make these financial statements more usable to different groups of investors?

And fifth is international. International coordination is very much on the Commission's plate. Just had a proposal on foreign registrants, and now there is a concept release on U.S. registrants. I think probably at least my initial suggestion is that we concentrate on the first four areas and wait a little to get into international coordination because we will then have the benefit of all the comments that will come in over the next few months on these two proposals.

So that's just an introduction to these areas, and I don't want to take up any more time. So we are now going to move to agenda item number four, which is comments on the discussion paper. And what I'm going to ask is that each member of the committee have an opportunity in five minutes or so to give their views as to whether these are good areas for the committee to look at, whether within these areas we should add, subtract or multiply issues and have a chance to give -- help scope out the work of the committee.

So I think our attempt here at the end of this session would be to reach more or less a consensus about what areas the committee is going to focus on and within that what are the issues that we are going to particularly try to analyze.

So we're going to go in alphabetical order here and I'm going to also use this opportunity just to introduce a little more the members of the committee. I think on the SEC web site we have the full biography of all the committee members, and we do have a very distinguished group.

So going in alphabetical order we're going to start with Denny Beresford, who is the Ernst and Young professor of accounting at the University of Georgia. Mr. Beresford, as many of you know, was chairman of FASB for a decade between 1987 and 1997. He also is a member of the audit committee of several large fortune 500 companies.

So I'm hoping that, Denny, you might be able to give us your views on the discussion paper and the issues before the committee. Thank you.

COMMENTS ON DISCUSSION PAPER

MR. BERESFORD: Thanks, Bob.

I think my comments are maybe just a little broader than the paper, but I hope they'll inform the debate. First of all, I'm extremely proud to be part of this important advisory committee and I thank Chris Cox for appointing me.

My colleagues and friends in Athens, Georgia thought this was a very big deal until they realized that the SEC reference had nothing to do with college football. But this is a serious issue we face today and I don't want to treat it lightly.

In the early 1990s when I chaired the FASB we developed our first notion of a strategic plan. The foundation of that plan was what we described as the three S's. Those S's stood for selective, simple and speed. Thus, the board and staff agreed that we needed to be more selective in choosing agenda projects and working only on topics that truly needed improved reporting, that we needed to simplify our standards in terms of complexity of solutions, length and understandability and that we needed to streamline our due process procedures.

We couldn't keep taking five years or more to develop new standards because outside support for change tends to erode over such a lengthy period. All board members signed off on that plan in relatively short order. However, as is clearly indicated by our being here today there was no real commitment to change by individual board members.

In the past four or five years following SEC and FASB initiatives on simplification and principles versus rules there certainly has been more effort on these confounding issues, but actual changes have been relatively modest, and other developments such as international convergence have created new challenges.

Thus we obviously need a fresh way of looking at the challenges and a new commitment to dealing with them. In short, while I am delighted that these high level resources are now being devoted to improving financial reporting we need to assure that this effort results in actions rather than just words. I certainly second what Bob said earlier.

At a recent audit committee chairman roundtable I attended, one of the members, the retired chief executive officer of a fortune 500 company gave his personal definition for the term GAAP. He said the GAAP means you need to follow this rule even though it doesn't make sense because otherwise you'll go to jail.

Now that's not exactly the highest form of praise for what has been an important part of my life for the past 35 years. My point in mentioning this is that I feel strongly we must deal with the relevance of current and proposed GAAP rather than just its complexity. Let me give a couple of examples.

I'm on the board of Fannie Mae. We use derivatives extensively to hedge the spread between a very large mortgage asset portfolio and related borrowings. As you know from a lot of press coverage, the excruciating details of hedge accounting under Statement 133 are too problematic and therefore the resulting recognition of gains and losses currently in the income statement doesn't come close to reflecting the true economic performance of the company.

As another example, in the FASB's forthcoming standard on business combination procedures, many aspects will be seen as nonsensical by businesspeople, particularly having to take legal and other directly related acquisition expenditures as current period expenses rather than being added to the costs of the acquisition and recording liabilities for less than likely legal contingencies at their supposed fair values and then marking them to market each quarter thereafter.

Can you imagine new tables in the Wall Street Journal listing current market values for lawsuits in process?

Complexity is a critical issue, and I sincerely hope that a number of actionable points will come from our committee's efforts, but we also need to keep in mind that accounting should be a practical activity. It's been described by the language of business and by some as a form of report card on a company's performance.

Using that report card analogy I can assure you that the system I've used to assign grades to students in the past ten years isn't considered perfect, but it's relatively simple and it's a good indication of actual performance. I hope that our work over the next year can help financial reporting better meet those same objectives.

Thanks, Bob.

MR. POZEN: Thank you, Denny. I guess I'd like to next go to Susan Bies. Susan was governor of the Federal Reserve Board here in Washington from 2001 to 2007. Before that, Dr. Bies was Executive VP for Risk Management and Audit at First Tennessee National Corporation. So she brings both a lot of knowledge in terms of the regulatory process and a particular expertise in the banking area.

MS. BIES: Thank you, Bob. Sitting on this committee, while I've been both the preparer and I served on the EITF and I've been a regulator, I've been asked to really sort of reflect the regulator's perspective on the various issues that the committee will cover. And I wanted to sort of lay the ground around some issues that maybe are a little unique from a regulatory perspective.

So let me just raise the issues. I'm not going to attempt to answer them today.

One of the challenges around the complexity issue, as already been mentioned is the fact that there are a lot of different users of financial statements. If we look at the banking system in the United States, we worry very much as regulators about something called moral hazard. We want the market, the depositors, anyone who has got exposure to a bank to bear the risk that the bank could go under. We don't want a safety net to be there which would require another bailout like we had with the S&L crisis of the '80s.

But the typical consumer has a terrible time understanding financial concepts in general -- witness what we're going through right now with subprime mortgages -- much less a corporate financial statement.

So how can we develop a framework that would allow a depositor to know how strong their bank is that they're choosing and yet provide the kind of information that regulators need and sophisticated investors in the market use -- those who buy the securities that are issued by the debt of those organizations. It's a real challenge, and also we have very complex organizations, very small little organizations. How do we balance the difficulty of the preparer's side of this too? And it's going to be something we'll talk more about.

The other challenge that I think we've got, and this really I think comes out very prominently in financial services, is that I think some of the places where we tend to have tension between preparers and some users of financial statements and I know around some of the standards that have been set in the past, really reflects the fact that we're asking preparers to put together financial information in a way that doesn't reflect how the business is managed or how a regulator would look at it.

Let me give you a couple examples. There is a big push to do fair value accounting around financial instruments. Now for trading book this makes perfect sense because it's got tremendous turn. It's going to turn a couple times a day and so you really want to know what is realizable and what's at the end of the day sitting there which will be your gains and losses tomorrow when you pick up the books and start running again, so it makes perfect sense.

Well, what about a loan book that is not destined to be traded? There is no borrower who will ever pay more than they borrowed or any penny more than the interest they owe on the loan. So when we do a fair value on something that's never going to be traded all we're doing is creating timing differences, and we need to ask, is this appropriate and how do we distinguish between timing differences that will reverse and what is permanently earned income?

Bank regulators are struggling with this on the definition of capital for banks because we have some things that flow through fair value mark to market and go through the earnings statement, end up in equity, that we know will disappear the next day. And so the quality of capital is very important when we look at the leverage of an organization and its ability to sustain surprises.

This also raises issues about the operations in a service business as opposed to just a financial instrument itself. Mortgage servicing rights, for example, the accounting says, when you create them, because you're going to service mortgages that are sold in the pool, you recognize all the gain up front.

Now during the dot com -- we got all upset when the dot com companies booked revenue from contracts up front. We thought it wasn't appropriate. And as a regulator I am concerned in the past that we were booking the fair value of the servicing rights without any regard whether that particular company had higher or lower costs to service or the quality of the mortgages or the size of the mortgages where they would actually -- more or less than the fair value, and so the operational numbers got mixed up.

And finally part of it is around risk. Markets are trying more and more to manage risk. I think some of the standards don't reflect current risk management practices. But more importantly we focus so much on a precise number and the precision I think implies more accuracy than we'll ever really accomplish in the world of financial instruments. And so we need to find a way to give supplemental disclosure around risks and make it more useful.

The last point I would like to say -- I really hope the committee does spend some time looking at technology. Two years ago the banking regulators did the first global project in the United States to have all 8,000 financial institutions use XBRL to do their financial reporting every quarter. We have found that this has greatly reduced errors. The processing time of call reports has gone from weeks to days, so errors are caught quickly. And it allows us to do very fast comparisons to identify outlier banks.

Now clearly we have a fixed format so it's a little bit easier than it's going to be for all registrants, but at least it's a lesson that says, "this is a wonderful new technology," and I would hope that we can help encourage that that goes forward as part of work that we do going forward.

And again, I thank Chairman Cox for nominating me and naming me to this committee and I look forward to working with everyone.

MR. POZEN: Thank you very much, Susan. The third member of the committee will be Michael Cook. Michael is the retired chairman of Deloitte and he is a member of the board of directors of a number of companies, and I would say that in every company where he's a member of the board he winds up being either on the audit committee or a chairman of the audit committee.

Mike and I also had the pleasure of working together at Fidelity, so I'm glad to have Michael with us.

MR. COOK: Thank you, Bob. Like the others, I appreciate the invitation to be a part of this group. I applaud the mission of improving financial reporting. I think that's very necessary and very important.

I also applaud the breadth of the charge and the breadth of the issues that are covered in the discussion paper. I for one have concerns that others do about complexity and delivery of information, but I would say those are not by any means the only issues that need to be dealt with -- and as promptly as some of these can be dealt with in the area of improving financial reporting.

For me they are part of the agenda but for me also the most important part of the agenda and a bigger issue is how do we make financial information, the financial reporting process more relevant and more useful to people who rely on the outputs of that system.

With that in mind I applaud also the charge to this committee that it is not limited to traditional financial statements or financial statement packages but rather the financial reporting process in the broadest sense because frankly I don't think in one year or maybe in the lifetime of many of us we can fix or deal with all the issues that exist with respect to financial reporting in the context of financial statements. We have to leave that to Bob and his colleagues at the FASB and colleagues at the IASB.

And hopefully some of those things can be addressed, but they are much more long term in nature than anything that we would do in one year. I would suggest the balance sheet is probably as illustrative of that as anything. It is coincidental today if the balance sheet represented the assets and liabilities of the corporation other than in accordance with generally accepted accounting principles.

That is a result of many, many years of flawed accounting for business combinations. It is the absence of intangible assets, the limitations of the historical cost model. Put all those pieces together, we couldn't fix the balance sheet in 12 months or even come up with meaningful recommendations so I would urge that we, as Bob has suggested, focus our attention. Likewise footnotes, a statement of comprehensive income and so on have a lot more work to be done with them than we could possibly take on during the time frame that we have in mind.

I do think the place that we can give some very serious attention and develop some meaningful recommendations is the financial information which flows from -- it is not the income statement, it's not the cash flow statement, but it is the financial information that flows from those statements and makes its way to the investor community through two other processes. And I think these are the most important financial communications today and the ones where our attention would be best focused.

One is MD&A. MD&A, notwithstanding the considerable efforts of the SEC, still is burdened by excessive amounts of legalisms and legal discussion and boilerplate. But notwithstanding that general limitation there is a lot of very meaningful information in the MD&A that tells people about the business and the future of the business and the liquidity in capital and things of that type that they would not be able to discern from the basic financial statements.

The information about important estimates and judgments and critical accounting policies is very useful, culls out the important from all the details that you find in the footnotes and says, this is what really matters to this company in preparing its financial reports.

MD&A, I applaud it, and I think we could give that some attention. I think the clear winner in the financial reporting sweepstakes today is the earnings release. This to me is where the companies that I am familiar with anyway provide the real information that is indispensable to the investor community.

The earnings release moves the market, often moves the market, often because it includes guidance. That's an entirely different subject, but it is rare in my recent experience that all of the GAAP-based compliance type financial reporting moves anything other than just confirming the information that has been previously issued through the earnings release process.

And here companies seek to put forth as best they can, and it is their best foot forward. I can say that as well.

What they believe is meaningful information about period to period performance of the business that can be used to understand the core and could hopefully be used to predict the future -- and this means culling out nonrecurring items, irrelevant items, trying to make period-to-period analyses comparable, and then in combination with what I think is of great importance, business performance metrics and indicators, when that is combined with adjusted financial information in an earnings release you have what I believe is really a very meaningful financial communication.

The question, you might ask, is are audit committees paying enough attention to those communications? Are the rules that govern those communications sufficient? Is there value to be had by having auditors involvement with those communications as opposed to the historical financial statements? What should those performance indicators be? How can they be defined? It is not necessarily where the attention is being given from a control and standards and process standpoint, but it is what really does make a difference.

So I would just close with a thought I've expressed in forums like this elsewhere, which is kind of my view of the irony of Sarbanes-Oxley and everything that came with it and 404 perhaps in particular is -- everything about

Sarbanes-Oxley has to do with playing defense. Everything has to do with auditing and internal control and whistleblowing and certifications, everything to protect the integrity of the basic financial reporting package during a period of time in which that basic financial reporting package has declined in value, and I would say declined rapidly in value in terms of its usefulness to the people who rely on financial communications.

So I have said, gee, it's time to let the defense take a rest, get the defense off the field and let's play offense. Let's see what we can do to improve financial reporting, which is what I think this group is all about. So I say I'm delighted to be a part of the offense. I will try not to be too offensive in doing it, but I think there is great opportunity for us to do things that will really enhance financial reporting and make all that effort that we're spending on Sarbanes-Oxley and 404 and everything else worthwhile because we'll be protecting something that really matters.

Thanks, Bob.

MR. POZEN: Thank you. And Denny, I think you'll be glad to know that there was some football learning here to be gained about defense and offense. I'm sure you'll convey that to your friends there in Georgia.

Now we have Jeffrey Diermeier. Jeffrey is president and CEO of the CFA Institute. This is the Institute for Certified Financial Analysts. And before he took that position he was the global CIO for UBS Global Asset Management.

So he is a very well positioned spokesman for the equity analysts who are surely one of the most sophisticated users of financial statements.

Thank you, Jeffrey.

MR. DIERMEIER: Mr. Chairman, fellow committee members, distinguished guests, Chairman Cox for nominating me, thank you very much.

So Mike, would this be the West Coast offense that we're trying to do here? A little run and gun?

Complexity, according to Webster's definition number two involves that which is hard to separate, analyze or solve. Simplicity, which is the black sheep of the complexity family, is, according to their definition number one, the state of being simple, uncomplicated or uncompounded. Uncompounded, interesting word.

It is my sincere pleasure to serve on this advisory committee as a representative of investment professionals for the purpose of putting forth recommendations to make financial reporting as uncomplicated and uncompounded as is practical.

I believe in the background section of the draft, Mr. Chairman, we should acknowledge several points. First, we know there are limits of course to reducing complexity. Corporate activities can be hard to analyze, particularly when derivatives or other complex financial instruments are utilized for hedging or even non-hedging purposes or when firms, because of their origins or cultures have unique ways to describe something that is inherently the same.

Where complexity is a natural result of business processes, it may be that disclosure is the only effective antidote.

Second, another critical driver of complexity in our system, and this is particularly relevant to something like CFA Institute where most of our candidates -- excuse me, right now we have more candidates in Asia than in the United States -- is globalization.

Back to our earlier definitions. If companies around the world had multiple reporting standards the difficulty in performing analysis or in multiple preparations is compounded. Comparisons can become challenged.

Investing is an act of relative comparisons. Over my 30 years in the profession I have tried but failed to understand what absolute value would be without reference to a set of comparisons or benchmarks. The draft paper, discussion paper we are commenting on today does a very fine job of laying out, I think, the five major items that the advisory committee should address. It is as comprehensive as it is ambitious.

The focus is on economic fundamentals. The statement that the two primary groups whose needs are addressed in financial reporting -- namely preparers and users -- is well put. The idea of setting these groups down in a best efforts basis where lobbying is minimized is important. I would offer two comments in that regard on that part of the draft.

First, the notion that preparers should want to reduce earnings volatility must be carefully interpreted. A key principle of risk management is that one does not artificially smooth those items that are inherently not smooth -- doing so invites excessive risk taking in what is called tail risk, and I know for a lot of time a lot of companies have been taught or told that it's important for them to reduce volatility, and they should try to reduce the business volatility but not the face volatility.

Second, users of financial statements also want information at reasonable costs. Despite a seemingly insatiable appetite for information from people like me, investors do not, as a general principle wish to burden firms with wasteful or expensive activities. A true owner would set out to achieve a proper balance.

I'd like to highlight some thoughts with regard to the five subcommittees. As regards delivering financial information, I suggest that the current business reporting model should be reviewed to include a set of primary financial statements that are cohesive and aligned with each other. That is, items reported on the income and cash flow statements could be specifically linked or aligned with those items reported on the balance sheet, although I give pause after hearing Mike's comments about the state of the balance sheet today.

In addition, sufficiently disaggregated information could be reported to enable end users to discern and understand different economic activities. Such information would include management's discussion and analysis of financial and nonfinancial information, including key performance indicators. Properly tagged, this detailed, cohesive information could be easily accessed using technology like XBRL.

XBRL looks like a good tool that if properly executed allowing for comparability across firms could be of great use.

In terms of substantive complexity there is a base appeal to the notion that standards would require the same measurement and recognition attributes for economically similar transactions and activities. As a principle, shouldn't accounting options be limited based on the economics?

As to audit process and compliance, the movement to principles-based standards is promising. Inherently professional judgment becomes a recurring part of the measurement and reporting process. Can't standard setters develop and promote a clear distinction between judgment and accounting choices? Could the need for bright lines and prescriptive rules disappear as standards based on principles accompanied by appropriate guidance are introduced?

Finally, in terms of the standard-setting process which ultimately provides the long-term framework that I think Mike was mentioning, I'd offer two comments. First, the least complex approach from a user or preparer standpoint, but certainly not from the standard setter's standpoint, would be to have one single global standard setter -- but because we're trying to be practical -- or its nearest equivalent.

Second, the standard setter should engage in a proper balance by inviting the primary preparers and users as well as the secondary groups mentioned, to provide the intellectual and experiential diversity like in this committee to ensure optimal decision making.

I look forward to working with the distinguished members of this committee as we attack the issues involved here today. Thank you.

MR. POZEN: Well, thank you very much, Jeff. That's a very wholesome explanation and you're representing well the group of analysts who have the "insatiable appetite for information." And I think they were very helpful comments.

We're now going to move to another committee member from the investor side, Scott Evans, who is executive vice president of TIAA-CREF. They are one of the largest pension funds in the United States, managing over $380 billion in assets. And Mr. Evans is well versed in investments and manages a big group there and I think is familiar with the general viewpoint of pension funds in this respect.

Scott, give us some remarks.

MR. EVANS: Thanks very much, Bob. Thanks for having me on this committee. I'd like to thank you and Chairman Cox for giving me the opportunity to represent the nation's pension funds in this important advisory committee.

As stewards of the long-term savings of millions of working Americans, pension funds serve a vital role in providing long-term investment capital to public companies. At my employer, TIAA-CREF, we manage the savings of 3.5 million participants in the academic, medical, cultural and research fields.

Like most pension funds we act in the direct interest of the beneficiaries that we serve in the capital markets. Pension funds represent the quintessential long-term owner for whom our system of public financial reporting is designed.

The FASB in its 2006 release, Conceptual Framework for Financial Reporting, states that the objective of financial reporting is to provide information that's useful to present for potential investors and creditors and others in making investment, credit and similar resource allocation decisions.

Since most institutional owners of public companies do not hold controlling stakes, we're dependent on management to communicate with us through the regulated medium of published financial reports and other public documents. As professional investors with a long-time horizon we are capable of making our own judgments and forecasts regarding future cash flows. However we expect company managements who act as our agents to communicate to us what they know.

It is far more important to us that disclosures enable shareholders to see the company through the eyes of management than that they strictly conform to a particular accounting theory or concept, for instance rules versus principles, stewardship versus decision usefulness. Although we're agnostic about these theoretical distinctions, we are passionate in our desire to improve the formal communication from company management to their owners.

Specifically we're hoping that this committee will rise above the temptation to focus narrowly on intellectual debate and seek instead to create a constructive climate where all interested parties work together to continually improve by testing and modifying approaches where necessary in an attempt to achieve consensus on taking practical forward steps toward our common goal of improved financial reporting.

As we embark on this year-long mission, I suggest that we keep several universal objectives in mind to test the relevancy of our suggested improvements. And I have five plays that I'd like to suggest for our West Coast offense here.

The first is transparency. As the steward of our assets, management should communicate what it knows about past and future state of company affairs to its shareholders. This communication need not be confined to financial statements but it must be timely and equally available to all shareholders.

The second is simplicity. Descriptions should be easily understood by nonprofessionals. Now as a Nobel prize winning former trustee at TIAA-CREF said to me just as I was about to talk to him about finance -- this guy was a scientist -- he said, "the greatest professors can always explain their work, no matter how complex, to any person, no matter what their background." Corporate managements should be able to pass this same simple test.

The third play is consistency. Communications should be consistent from one period to the next.

Comparability, users should be able to compare one company's disclosures to those of users in similar fields of enterprise. All attempts should be made to fully utilize technology like XBRL, to make data available in standard format for quick and efficient dissemination and analysis.

And last but certainly not least, accountability. Because of the separation of ownership and control, managers of public companies are accountable to those who own the capital. Owners deserve to have enough information to evaluate the effectiveness with which their capital is being managed and at the same time management needs to be free to communicate their story in their own words. Overly prescriptive reporting requirements may serve to undermine the effectiveness of this communication.

I look forward to working with this esteemed group over the next 12 months, to recommend solid and lasting improvements in the reporting mechanisms that managers and owners use to communicate with each other. Thank you very much.

MR. POZEN: Thank you.

Now we move to the next person on our list, who is

Linda Griggs. Linda is a partner currently at Morgan Lewis, a Washington law firm. She also was at one time Chief Counsel in the Office of Chief Accountant, so we're glad to have you, Linda.

MS. GRIGGS: Thank you, Bob. I appreciate being named to this committee to represent securities lawyers. I also serve as chair of the law and accounting committee of the American Bar Association, so I expect to be able to use that committee to assist me in this endeavor.

I commend the Commission for forming this advisory committee. The financial reporting system in the United States has played a critical role in the making of the capital markets of the United States, highly credible, efficient and effective.

While our financial reporting system has been a gold standard, as Conrad mentioned, during the last 10 years financial statements have become increasingly difficult to prepare and to understand. These changes have resulted at least in part from the increasing trend towards value-based accounting, the clamor for more objective accounting rules to confront our litigious society and increasing complexity of transactions, including transactions involving multiple elements, requiring significant analysis to determine the timing of recognition and complicated products designed by ingenious investment bankers to address companies' economic or financial needs.

For several years regulators, standard setters, accountants, investors and academics have expressed concern about the increasing complexity of accounting standards. Some have also questioned whether reported financial information continues to be useful and to reflect economic reality.

In an effort to reduce complexity the FASB has begun to adopt principles-based accounting standards. SFAS 159, which permits companies to elect the fair value method of accounting for certain financial instruments is a recent example of a principles-based standard. But some registrants fail to understand those principles when they tried to implement FAS 159 and perhaps some of that failure to understand was because it's difficult to articulate principles.

Principles-based accounting standards requires an enormous effort by the standard setters to really articulate those standards in a way that people can interpret and follow. I believe that it is appropriate and timely for a thorough examination of ways to ensure that our financial reporting system continues to provide transparent and meaningful information to both preparers and users of that information without adversely affecting the ability of publicly held companies to compete in the global market.

The scope of the review contemplated for this committee is broad, perhaps impossibly so, but I believe it is consistent with the seriousness with which the commission views its mission of ensuring appropriate financial disclosures. I personally believe that our consideration of the benefits and disadvantages of the mixed attribute financial statements is crucial to rationalizing and increasing the transparency of our financial reporting system.

The establishment of a new value-based financial statement is an option that I think we should carefully consider. I also think we should consider whether there are ways to provide more meaningful financial information to investors. For example, should the financial disclosure rely more on information about the financial elements of business transactions rather than on the single bottom-line effect of those transactions and should the Commission's rules encourage or perhaps even require that the information in those press releases which, I agree with Mike Cook, have become increasingly the method by which managements tell their story? Should that information be required in SEC filings instead of now where there's almost an apparent discouragement of non-GAAP financial information to be in public filings?

Finally, no consideration of improvements to financial reporting can ignore revenue recognition. One of the areas that has resulted in considerable enforcement action and may account for some problems for companies trying to compete in the global marketplace -- and I think we also need to look at the reasons for and the appropriateness for all of those restatements, the 10 percent of the financial statements that have been restated in the last year.

I look forward to working with Bob Pozen and the other members of the committee and the Commission Chief Accountant and Director of the Division of Corporation Finance and their staffs as well as the observers to the committee from the FASB, the PCAOB, the IASB, the Treasury and the Federal Reserve.

I think we can work on recommendations to improve the financial reporting system, and I look forward to this work. Thank you, Bob.

MR. POZEN: Thank you, Linda, for your intelligent and very thoughtful comments. I should have mentioned that you were head of the law and accounting committee at the ABA. I'm sorry I neglected that.

Now we have Joe Grundfest. Joe is, besides being a personal friend of mine, a distinguished professor at Stanford Law and Business. He's codirector of the Rock Center on Corporate Governance. He served four years as an SEC commissioner and he is likely to spark the most discussions by a few very interesting remarks.

MR. GRUNDFEST: Interesting is always an interesting word in that context.

So let me begin, Bob, with two rhetorical questions that I offer for the purpose of perspective, and I'd like to pose to all of my fellow panelists. First question, who among us can name the great -- the truly great federal advisory act committees of all time? Okay. Second question -- my point, all right. Second, which committees have advanced the ball to make meaningful and lasting contributions and how and why?

Aha. My guess is that the vast majority of us can't think of a single federal advisory committee act committee that has actually made a meaningful and lasting and long-term contribution, and I suggest that we contemplate the reason why that is the case, we learn from that history and we do what we can, which may or may not be very much, to do our best to avoid that destiny.

And I think one of the important prescriptions that we need to follow is along the lines of one of Bob's favorite sayings here, is that we can't let the perfect be the enemy of the good, that I do think we have to be very focused and pragmatic in terms of what it is we're attempting to accomplish. I think it is improbable that we will be able to solve all of the world's problems in 12 months through this committee, but I think it would be wonderful if we could advance the ball in an effective and pragmatic and doable way.

In other words, if we set the bar for ourselves low enough we will succeed, all right. And I strongly recommend that we have very, very -- from that perspective, low but useful expectations of ourselves.

Now with that by way of a rhetorical introduction, let me share with you one procedural suggestion and then five substantive observations. First a procedural suggestion.

We are not the fount of all knowledge and wisdom with regard to the issues that we are going to address. I understand that we have a web page, and that's really very lickety split and very nice. I think we need to figure out some way to make it easy to have people who are knowledgeable and want to share their views about the topics that we're wrestling with, share those views with us, whether that's some kind of incoming feature, setting up a blog, what have you.

We can all talk about that. But there are lots of other professors, students, knowledgeable people out there who probably have good ideas that they want to share with us about topics we're wrestling with. You know, my view is let's open it up. Anybody who's got a good idea, I want to hear it, and I want to figure out what we can do in order to incorporate those ideas. So opening the tent that way I think is really going to be very important.

In terms of five areas where I think we can really make substantive contributions within that year and maybe go down as one of the great federal advisory act committees of all time -- the hall of fame. Remember, it's a small hall of not very much fame, all right; we'll call it the hall of non-ignominy.

The five substantive areas are in the following regions. One, probability. Two, technology. Three, liability. Four, theology. And five, formality. Very briefly.

First, probability. It is true that you cannot take a clear picture of a fuzzy object, yet financial statements repeatedly call for point estimates of probability distributions, therefore by definition financial statements always force you to lie, all right.

Take the simplest example, cash. How much cash do you have? Well, if you're in a big organization you can come up with a pretty tight point estimate of how much cash you have, but it's really a probability distribution with a very small variance. What are your securities worth? Well, you're forced to give a point estimate of a probability distribution. Depending upon the kind of security it's either a tight variance or a huge variance. We have no mechanism for honestly describing the uncertainty that pervades all of these numbers.

Forgive me, that's preposterous. We're forcing people to give false representations of reality. We need a way to describe the probability estimates that are inherent not in some of these numbers but in all of these numbers.

Second, technology. We've heard for years now about the potential value of XBRL and there are situations where XBRL is being picked up and is being used to very great advantage. The banking industry where, number one, you've got highly standardized numbers, and number two the numbers are mandated. XBRL is not being picked up in the rest of the environment at any sort of meaningful pace at all.

XBRL is currently I think headed towards the fate of Esperanto, a better language that nobody speaks, all right. What we need to do is figure out how to handle the Esperanto problem for XBRL, and those of us who come from Silicon Valley and the software world, there's lots of great technology that never winds being picked up and adopted because it fails the marketing test.

XBRL is a marketing failure and a technological success. There are ways I think to go about turning it into a marketing success and I think what we need to do is have this committee look at ways to jump start adoption in that space.

Third, liability. If you think that the financial reporting process is not conducted with everybody looking over their shoulders and thinking about the possibility of being sued by the SEC or private class action litigation or what have you, you simply don't understand the reality.

The definition of GAAP that was earlier offered -- rules you need to follow even though they don't make sense because otherwise you will go to jail -- is a pretty good operative definition of GAAP because it's hard to explain them through any other coherent logical process. To the extent that this committee can help provide the judicial process with a better understanding of what's important and what's not important so that we can really drive meaningful information and take the liability second guessing out of the process -- I think that would be a great advantage.

Fourth point, theology; rules versus principles. Forgive me, but give me a break, all right. The reality is sometimes rules are best, sometimes rules are absolutely necessary. Other times standards are best. Sometimes standards are necessary because you really can't write rules.

It's also true that standards often as they are applied devolve into rules. Easy example, take the most standard-based principle in the law, the notion of a fiduciary standard. Well, you look at the Delaware jurisprudence applying the fiduciary standard to takeovers and you realize that when it comes to breakup fees that standard has devolved into a rule, but if you keep the fee at less than three percent you're generally okay. You apply a standard often enough it generates a set of rules.

I think our goal here should be to try to get past the rules-principles rhetoric because I don't think it gets us anywhere and to try to explain when you use rules, when you use standards and how standards can intelligently be applied. And this is an area that of course feeds back into the question of liability in a very important way.

Last and maybe most important, the whole issue of formality. And by formality I mean the distinction between recognition and disclosure. Recognition means you got to take a number and you've got to plug it into these GAAP financial statements. Disclosure means you can take the number and disclose it in the footnotes or someplace else in the SEC filings.

Ladies and gentlemen, the reality is that some of the biggest battles arise when you move from disclosure to formal recognition. Once you go from disclosing the information, whether it's in MD&A, to forcing it to flow through the income statement.

There are ways, I think, where we can increase the credibility and the usefulness of nonrecognition items in a manner that can help diffuse the politics of some of the recognition process, can help address some of these issues. And one question that I do think is fair for us to consider is whether we're asking the financial reporting process as formally defined by GAAP to do too much, for it to be answering to too many different masters and for it to actually try to estimate the real economic value of the business.

I don't think that that can be done. And if you ask somebody to do something that's impossible the odds are they will fail. And I think by setting that set of standards and objectives for the formal recognition reporting process we're putting our brethren in the accounting profession in a very, very difficult position because we're asking them to do something which has to fail.

So let me close very briefly by saying there have been several references to the West Coast offense. As a representative of Stanford where we lost Coach Walsh who is the inventor of the West Coast offense, let's remember the basic football philosophy -- short passes down the field with higher probability of success, that's what I suggest. If we complete these five relatively short passes we can score some points. Thank you.

MR. POZEN: Thank you, Joe. We'll definitely take your advice.

Now we have Greg Jonas. Greg is managing director of Moody's, one of the most prominent credit rating agencies. Before joining Moody's he was at an audit firm and he also is -- at one point was executive director of the AICPA special committee on financial reporting. So we are glad to have Greg, who obviously has an interest in debt securities as well as equity securities. Thank you.

MR. JONAS: Bob, thank you. I'd like to echo first the comments that others have made about what a privilege it is to serve on this committee, and I appreciate very much the opportunity to do so.

Over the years I've had the pleasure of working with and for many of the people who are at the table here today, and I can assure all of you that I am by far not the brightest person in the room. My only hope is that being fairly simpleminded and deliberative about these things is actually an advantage when you're thinking about taking complexity out of a system.

I have been a student of financial reporting now for -- I hate to admit it -- about 25 years, and I have never seen, in that time period, such a critical time in the history of financial reporting. I think there's four reasons for this.

One is I've never seen a time when we have so many big ticket fundamental issues that are in play in the financial reporting system. For example, as we speak, standards setters are debating what things get put on financial statements, how we measure these things, when they get taken off, how the display of financial statements ought to look to the reader, whether we should set principles or rules, and then throw in a couple minor little projects like rethinking leasing accounting and pension accounting and then some absolutely mind-numbing reconsideration of the foundations on which our models are based.

The second reason why I think this is a critical time is globalization of everything, including financial reporting. And I think what globalization is doing is it's calling in question the institutions that we have that were built at a time when each country had their own structures and their own institutions to support financial reporting. And we are calling to question whether those institutions are still relevant today.

A third reason why I think we are at a critical juncture are all the changes in the economy that have occurred over the last 25 years and among them globalization of markets, technology and unprecedented level of innovation.

And the fourth reason I think we find ourselves at this critical juncture, and frankly the critical reason why I think we're gathered around this table, is the unprecedented level of regulation in cost and weight that we have now before us in the financial reporting system.

I think what's occurred is that we have made improvement upon improvement upon improvement for 40 years and we've never stepped back and said, "does it all make sense in totality as a system?"

Two analogies come to mind. Many years ago I was involved in shop floor layout design, and it would not be uncommon to go to a factory floor and you'd absolutely see literally a spaghetti diagram of processes and techniques in place on the floor. And you ask, who would have designed such a thing of spaghetti? And the answer is, no one designed such a thing; it happened piece by piece by piece with each piece being relevant and well intentioned but the totality never being examined.

What we did in those days was eliminate, simplify and focus as a means to then improve. It was a necessary precedent to allow additional improvement -- was to take out weight.

A second analogy that I have happened to me just earlier this week, and we've all experienced this. You know, your computer slows down. The darn thing doesn't go as fast as it used to and it does it because your hard drive, I'm told, gets all clogged up with stuff. And then you got -- you're hanging on to too much stuff and so you got to defrag the hard drive, whatever that does. I think it allows the computer to put things in more efficient space. And then you delete all your stuff that you don't need anymore.

And so I think, you know, we need to defrag here a little bit, again, as a way to improve and make room for improvement. And I believe we need improvement.

There are four areas that I think this committee can add particular value. One is reducing complexity, and I am most optimistic about our ability to do this because to my knowledge no committee such as this has ever gathered specifically to tackle that thorny issue. It has always been an afterthought.

You know, everybody likes to reduce complexity, but it has never been anybody's first job. This needs to be, in my mind, job one.

Second opportunity for help is delivery. I really think, because of technology, we can really improve how investors access information in a manner where one size does not fit all, which has been the traditional way we've delivered financial information forever.

The third area I think we can add value here is by making suggestions for a globalization of institutions critical to the financial reporting process. This is all new to all of us. Everybody is thinking about this now. The SEC is going to get a mountain of input very soon on these critical topics. I think we need to be a voice in that area as well.

And then finally I believe we can help with what I call excessive short-termism in the market. In my job at Moody's I often find myself listening to companies present their business plan to discuss their operations as they update us on the status of their financial affairs, and it is very, very often the case that at some point in the conversation the company almost confesses, although they don't mean it in that way, but it's kind of a shameful kind of thing that they say I'm having to take some short-term business actions that really are not in the long-term interests of my business.

And I think I'm not one who says we need to shoot the short-term investor. I think what makes a market is the fact that there are short-term investors and long-term investors. But I do believe that people tend to focus on the short-term in large part because we are not giving them the indicators that they need to really understand the value creation process and how that relates to the long term.

So I greatly look forward to our many discussions and working with this group, and hopefully I can add some value along the way. Thank you, Bob.

MR. POZEN: Thank you. So we can defrag and decipher. We now have Chris Liddell, who is the CFO of Microsoft. Chris is responsible for Microsoft's worldwide financial organization. Before joining Microsoft he was the

CFO of International Paper, and he also was chief executive of Carter Holt, which is New Zealand's second largest listed company. I say that because you'll notice that he has a little bit of a Kiwi accent still in his presentation. Thank you.

MR. LIDDELL: Thanks, Bob. I wanted to first commend the SEC for bringing together a multi-disciplinary group like this to address what I consider to be a critical topic. I am personally delighted to be a member of the Advisory Committee and believe we have an extremely important task in recommending improvements to financial reporting.

As the background paper notes, the U.S. capital markets are the deepest and most liquid in the world and we have a collective responsibility as committee members over and above our individual roles to ensure this leadership position is retained.

Clearly, I do not want to prejudge any of the recommendations; however, I do have some preliminary observations. As chief financial officer of Microsoft, one of my main responsibilities is to communicate with our owners; and in doing so to ensure that our financial reports reflect the economic substance of our business.

When reviewing the discussion paper, I was struck by the fact that the need for financial reports to reflect the economic substance of business was listed as an objective for each of the participants in financial reporting, and I fully endorse it as our primary objective.

I also agree with the other stated joint objectives that all participants should want clear guidelines that allow financial reports to be prepared and presented in a straightforward fashion, do not want reports to be subsequently deemed to be incorrect, and do not want companies to spend too much money in management time in preparing financial reports.

However, I see these as secondary and contributory to the primary purpose of clearly and as accurately as possible conveying economic substance. Further, what is critical at all participants' interests should be considered, my belief is that investors are the foremost group whose interest should be optimized for, especially where interest might conflict. I am an open advocate inside my company for shareholder value, and never lose sight of the fact that they are primarily to serve the interest of our shareholders.

I agree with the proposed areas of inquiry and the subcommittee's structure and focus. In terms of approach to what is clearly a diverse, complex, and multi-faceted problem, I take the same approach that I would inside our company and recommend a three-tier structure for our recommendations.

The first tier is what I described as "no regrets changes," which have relatively no implementation costs and have a high degree of unanimity amongst the various stakeholders and participants. The second tier would be more ambitious changes that may have greater impact, but would also possibly have more substantial transition issues and/or suboptimal impact on some of the secondary stakeholders.

Lastly, I would put up what I described as game changing ideas that may have significant implementation issues and may require more study after the term of the Committee, but which hold the promise of not only continuing the U.S. capital market's current status, but in fact, extending its leadership position. My only caution is that any recommendations clearly consider any transition issues, have a long-term approach, i.e. that they be sustainable over a long period rather than be continually modified, and work well both in concept and in practice.

For example, we should resist changes which have the appearance of benefit, but whose costs are greater than those benefits and hence are not only unsustainable, but also not in the long-term interest of investors. Furthermore, all companies, even large ones, do not have unlimited human or financial resources. And, even if a recommended change passes the cost-benefit test, it should pass the secondary test as to whether it is the best use of those resources.

In terms of my role, I look forward to contributing my experience, perspectives, and ideas to the Committee, and once again thank you for the opportunity to participate. I look forward to our further discussions.

Thank you.

CHAIRMAN POZEN: Thank you, Chris.

We now have remarks from Bill Mann. Bill is a senior analyst at Motley Fool, which I think represents a very important perspective of the individual investor and has put out an investment newsletter through the web and are I think very tuned in to some of the more recent developments about the dissemination of information.

Thank you.

MR. MANN: I am also from North Carolina, which is a basketball State. So if you all could explain to me the football analogies later, I'd really appreciate, because they are all just beyond me.

(Laughter.)

MR. MANN: Unlike most of the people here, my primary access and use of accounting has been as a consumer throughout my career and being at the Motley Fool and being as someone who picks stocks and recommends stocks to individuals, I see all the time the anxiety the people have that things are being hidden from them, that things are not being communicated, that managements are able again to hide things in plain view.

I think a very important component of this Committee, and it's been brought up a number of times, is that financial transactions are simply more complex in today's age. You know, I think as an allegory the Declaration of Independence was written on a single page, whereas, the regulations for footings or cement barriers in Fairfax County run 40 pages, which unfortunately I now know a lot about.

One of the interesting things -- we are in a fairly unique time. And the Motley Fool has been a company that has taken advantage of it and I believe has really assisted individual investors. And that is the rise of technology. If you think 15 years ago we had very limited access to documents, I think the technology has increased people's access to information.

But, I don't think it has increased people's levels of understanding of the financial documents or the information that's supposed to be put forth. I think that we're missing an opportunity to communicate to owners in a way that's useful to them and so I am delighted to that end to see the scope of Section 4 of our recommendations or of the position paper. Here's why.

We do a number of surveys and we've seen this over time; that less than 30% of all individual investors bother to read the annual reports of the companies that they own. I actually think that the number is a little bit lower because even in an anonymous survey it's probably a little bit embarrassing to say that you do no more research on the companies that you own than you would the television that is in your living room. This to me is just horrifying.

In my role in speaking to our five million members and readers and people who access information through the Motley Fool, I wish I could say that I've received a lot of recommendations from individual investors about what would make the financial statements more useful. But I really haven't. Instead, I have a message that individual investors have in some ways given up.

There's a lot of cynicism. The companies are hiding things. This doesn't help any of us in the capital markets. One individual investor who I think a great deal of is named Michelle Leder. She writes a web site called, "footnoted.org." Basically, she finds opportunities and pitfalls in businesses by combing through the footnotes of financial statements. She's very good at what she does. And when I asked her about some of the things that would make financial reporting more simple, she said, "It would be simple. All you need to do is put me out of business. I should not have to do what I do."

Individual investors are not financial professionals by and large. That said, many of them are extremely sophisticated. I think it's folly though to think that any investor is going to read a 500-page 10K, which many companies now are routinely turning out. I think that there is an enormous gap between the press releases, which, as has been mentioned, is the thing that tends to move the market and the filings themselves.

I think the SEC did a very smart thing a few years ago in reminding companies that they are liable for misstatements or for fraud in their press releases. However, one of my colleagues still describes company press releases as a game of fetch; as in, here's the ball, don't look anywhere else.

We have a tremendous opportunity here with this panel, particularly with the MD&A section of 10Ks. As part of the formal financial filing, it's an area where managements need to know that they have a lower level of legal liability than they do for say the audited financials. So I think about the comments that Mr. Cook made about the balance sheet. How helpful would it be for investors if management had the ability to give their own informative opinion of the current value of its assets in the context of the MD&A.

So, it's a delight for me to be here and I am honored to be working with this Advisory Committee.

CHAIRMAN POZEN: Thank you, very much, Bill.

We now will hear from Ed McClammy. Ed is CFO and Treasurer of Variant, which is global technology located in Palo Alto. He's also served at the other companies, Quantum and Lucky Stores, and at one time worked for an accounting firm. He is representing mid-size companies.

Thank you, Ed.

MR. MCCLAMMY: Thanks, Bob.

I'm pleased to be representing small and mid-sized companies on the Committee. Clearly, I feel that the small and mid-sized preparers have suffered probably the most burden from the increased complexity of the financial statements. And also coming from the perspective that I have a background dealing with most of the elements in developing the financial statements and started my career with the FASB. So I've been on the standard setting side with a major auditing firm and a preparer, and as an individual investor, at least, from the investor perspective.

So, primarily coming from today, I could talk about this for hours coming from a mid-sized complex company that's had to deal with the complexities.

CHAIRMAN POZEN: Well, we're not going to give you a few hours. Let's have the shortened version.

(Laughter.)

MR. MCCLAMMY: I probably won't even take my five minutes today, so, just a couple of points that I want to make. And when I think GAAP is being set by too many sources, clearly the amount and complexity of items that are coming out of the FASB, the emerging issues task force and the SEC from a formal basis have grown. But there's also, I'll put "GAAP" in quotes. There's also "GAAP" being generated, whether intended or otherwise, through SEC comment letters, either from and I say intended from sending messages or from people reacting to a comment for expediency sake in getting a filing done or otherwise, where I think they're agreeing.

And it may not have even been a point the SEC was making. Personally, I think in a lot of cases, it was probably just a question that people are adopting, and the major accounting firms are spreading through their organization: here is the SEC's thinking. If you don't want to comment, you should adopt this either in your disclosures or in your accounting.

So I think there's a lot of "GAAP" being created through that process and in addition to that we now have the Oversight Board, who I think again intended or otherwise are through their review processes creating GAAP from comments that they raised. That the accounting firms then roll out and say, we need to adopt this as a standard for "GAAP," or the firm could have a problem when the Oversight Board comes in for the next review.

So I think there's a clear sign of complexity that comes out of all of this when we ask accounting firms for advice on an accounting issue; and the local partners who deal with this all the time cannot give us an answer. They either have to go back to a subject matter expert or they have to go back to the home office. And I think through that process of going back to those people, we talked about having a view on the economic reality or reasonableness.

I think it turns into more conservatism as you go through that process, and we lose some of the economic reality as we go through it. Because all of a sudden everyone becomes concerned about being second guessed as they go through various review processes or being sued if something turns out to be different than the most likely outcome.

For an example of where I think second guessing has come in, I remember when I was in public accounting and helped companies prepare 10Qs, and they may have been five or ten or maybe even 15 pages long. They were very easy to pick up either the one you were looking at, or from a CFO's perspective to pick up the 10Q from a competitor or some other industry we were looking at getting involved in, and to fairly quickly get an update to what had been in the 10K.

And I think nowadays, because of all the second guessing and different requirements, it is more difficult today to get through a 10Q than it was to get through a 10K several years ago, which I think is a reason why more of the 10Qs and 10Ks are going in the trash can than are being read. I think the other thing this complexity has led to is more people relying on earnings releases, investor conference calls, and also relying more on an adjusted non-"GAAP" information than on "GAAP" information and SEC filings.

Several committee members have said, I think people feel like they get more reasonable, useful information from those sources, and more timely than they do out of the SEC filings with formal "GAAP" technical answers. So I think this is a clear indication that we have a problem and that the problem needs to be addressed. And I am pleased to be part of that.

Thanks, Bob.

CHAIRMAN POZEN: Well, thank you, Ed, for your very specific and concrete remarks. I tend to agree with you a lot that we have probably too much of GAAP running around and we need to sort of figure out what is and isn't GAAP and grab hold of it.

Now we have Ed Nusbaum. Ed is CEO of Grant Thornton. Sometimes it's called the small audit firm, but I think, more properly, a middle size firm that isn't quite in the big four. And Ed is representing auditors of middle-size and smaller companies. And I look forward to his remarks.

MR. NUSBAUM: Thank you, Chairman. First of all, like everyone has said before me, I am honored to be on this Committee and thank Chairman Cox for inviting me to join the Committee. I am particularly pleased and actually a little surprised with the consistency of the comments so far. We all seem to be sharing a lot of the same thoughts on what we need to do to improve our financial reporting model to eliminate complexity and to advance the process forward with simple focused ideas that can be accomplished.

I particularly think that Chief Accountant Hewitt addressed and laid out very clearly the issues of terms of complexity, in terms of the increasing number of restatements, and extending the role of this Committee to the usefulness of financial information and the need to improve the usefulness. And, particularly, his comments about looking at this with an open mind and a blank sheet of paper, which I think is exactly what we need to do. I believe that the paper you circulated, Chairman Pozen, does accurately state the issues. It provides a framework for where we need to go forward, and I think it provides a basis for us to commence our work.

Unfortunately, business has become infinitely faster, more complex, and more global than it has ever been before in our history, and we need to address that with our financial reporting model. The economic, legal, regulatory, social, and technological changes have combined to threaten the relevance and reliability of the current model for reporting business and financial information. As an auditor, I see our work as a cornerstone for insuring the integrity of our capital markets.

We need the consistent flow of accurate and timely information to investors in order for them to make decisions; and, it's a three-pronged role. And that is, first, of course, the management to the preparers to share the responsibility, and as others have said, to prepare thoughtful and useful information. The auditors to assess the reliability of that information in a timely way and in a way that satisfies the needs of the users. And, finally, it's also the responsibility of the investors to help us formulate what information will be useful, whether it's performance indicators or information in press releases.

One observation is that coming from a firm, be it small in the eyes of the beholder, I guess; a firm that focuses on small and mid-size public companies in many ways. The world has changed in another way, and that is that the purvey of global operations used to be in the very largest of companies, but today, most small and mid-size public companies have international operations and have become global in their nature. Indeed, most private companies had become global in their operations. So we need to take a global view in applying standards in everything that we do.

The convergence process for accounting and for auditing and other standards is a step in the right direction, but we need to accelerate that pace. In 2002 our firm Grant Thornton called for a global, principles-based approach to all standard-setting areas: accounting, auditing, and ethics standards. That need is even greater today. Those standards need to be clear, concise and appropriate, whether they're principles-based or have some rules within them. And I think we have to clarify that process.

The process for setting standards can be and should be improved, but I think one of the factors that has been mentioned by almost all of the people on this panel is the fact that hindsight is 20-20, and we have entered into an area where second-guessing has impacted our ability to produce accurate and timely financial information. Excessive exposure to legal liability and second-guessing, I believe, limits management's desire and the auditor's desire to provide transparent and useful information on a timely basis.

The number of restatements, and particularly the number of restatements with the smaller and mid-size companies, the non-accelerated filers, which have been increasing at a much more rapid pace than it has been for accelerated filers, is an indication of the problem associated with the complexity and the other issues impacting second-guessing.

Going forward, I think the key was mentioned earlier, is how do we provide useful information on a broader basis to the users of financial information, information that they need for decision making. Financial statements and the audit reports do not currently provide the information necessary to make decisions, and we need to take a positive step through performance indicators and other information, useful financial information, using technology and items like XBRL to enhance the business reporting process.

I have been in this business almost 30 years and I am proud of the accomplishments at Grant Thornton and the advances the profession has made. But I think as Greg pointed out, now is the perfect time to look at all of those incremental advances that we have taken as a profession and reassess them so that we can come up with a better business reporting model applied on a global basis.

Thank you.

CHAIRMAN POZEN: Thank you, very much, Ed.

And now, in alphabetical order, we come to Jim Quigley, the other representative of definitely a large audit firm, Deloitte Touche. And Mr. Quigley has been an auditor of many large and multi-national companies, and he is a distinguished representative of the large auditors and as I said presently at Deloitte.

Thank you.

MR. QUIGLEY: Well, thank you, Bob.

I am delighted also to be a part of these discussions, and I am delighted to represent the auditors of the large multi-national companies in this process. As has been stated repeatedly, I believe investor confidence is essential for the effective capital markets. And I think those rely on and require relevant, reliable financial reporting and as has been said repeatedly, our current financial reporting system is not as effective as it could be, for sure. And I would even suggest that at times this system is in gridlock.

I am hopeful. I would like to be optimistic, but I am at least hopeful that our discussions will lead to recommendations that will improve the effectiveness of this system. And, I also believe that we need to consider the work of prior groups that had similar charters and try to understand why were those recommendations not implemented. And if we understand those obstacles, I think we can increase the likelihood that we can develop recommendations that will in fact find their way into implementation.

It is a unique opportunity for the accounting profession to be part of a broad-based group to study and contribute to what I hope will be meaningful solutions and some recommendations again that we can implement. I think we need to examine the root causes that have led to this complex model that we have today, and I believe we need to look at the system if we truly want to be able to make improvements. The checks and balances that are referenced in the discussion paper are clearly in place. And I think if we don't look at the system, we're not going to be able to clear the gridlock out of the intersection.

It isn't simply about, let's have standard setters do 'X'. Let's have preparers take this action. Let's have auditors do this, or let's have regulators take some other action, because if in our effort at focused recommendations we look narrowly at only one participant in this system, I think there will be so much resistance to change that these recommendations won't find their way into implementation.

I also would like to see us through this process. Understand the sources and the nature of the escalating restatements that have been referenced. I think both the number and the type of restatements are a very important symptom of the gridlock that I refer to, and I think the restatements themselves are in fact a flashpoint that has contributed to the formation of this group. Is today's concept of materiality operational?

I looked at a recent study of restatements and less than 25% of them constituted a material restatement that is a material remeasurement of income by traditional measures.

And can we create an environment where reasonable judgments are both encouraged and then not second-guessed? I know the fear of second guessing influences the thinking and the actions of very talented professionals who have made this their life's work. And to come to a conclusion you do have to rely on subject-matter experts and the consultation process that has been referenced, it simply slows the process.

But yet I believe the complexity of the model we have today actually compels that, as well as the penalties that are inherent in that process. It's easy to advocate the principles-based system. I acknowledge the limitations that were earlier referred to with respect to limiting ourselves to such religious debates, if that's the right way to describe those. And it's easy to also become a strong advocate of encouraging professionals to exercise their judgment.

But I believe as long as we have a rules-based approach to regulation, a rules-based approach to enforcement, a rules-based approach to litigation, a principles-based system, and one that is underpinned by professional judgment, will remain only an aspiration. Thus, the reason that I think we have to look at this total system, if in fact we want to impprove its effectiveness, I am hopeful that we will be able to develop actionable recommendations that will help us clear this gridlock and improve the effectiveness of the system. And I look forward to being part of the discussions and participating actively to try to accomplish that objective.

Thank you, Bob.

CHAIRMAN POZEN: Thank you, very much Jim. Now we will have remarks from David Sidwell. David is the CFO of Morgan Stanley and before that spent time at an audit firm. He obviously is very well-versed in securities markets representing securities brokers and dealers.

Thank you, David.

MR. SIDWELL: Thank you. I'm glad you didn't use the word "investment" bank, based on a prior commentary.

(Laughter.)

It's also unfortunate having lost many of the comments which have been so good have already been said, so I am going to keep my comments short. I really would like to add to everyone my thanks to being invited to participate in this. It is an honor. I also think the paper you have prepared is well-written. I think the approach is good. I do also agree with the comment you made at the beginning, Bob, that we really do have to come up with a doable set of recommendations. This could be boiling the ocean, and we have to avoid doing that. Let's make some progress on those things we can make a difference on.

A number of commentators have also mentioned by way of process that we should get input from other groups and I think that is hugely important. This is not a new issue and there are many people who have ideas and thoughts that we could find very useful. So I do think we need as a process matter to find ways of soliciting and considering the thoughts of others.

Two opening statements would be that I do actually think the case of change is very well made, so hopefully we won't have to spend much time on saying, is there a need to do something differently. I think we have heard, and it was very encouraging that Chairman Cox and Con made the statement so clear about the mandate of getting this issue of complexity. As a preparer and the other preparers at the table may join me on this, it's little disheartening when you produce 120-page documents, which you have enough difficulty understanding, and if the actual investors don't find it useful, that's not our goal.

We want to have as preparers a good dialogue with investors, a good dialogue that really is explaining what we're doing as a business and the trends we see. It is not to get mired down in the complexity of a footnote that is hard enough as a preparer to understand, and I am sure, it is much more difficult for an investor.

I think we also would probably agree that the goal is pretty simple. It should be sustainable, good financial statements, good disclosures which facilitate the capital markets. The issue is actually how you get there. I think in terms of doable for me, there are a few errors in focus. I do think that the time is right when you think about the work FASB is doing on conceptual framework, the work that is going on with the international standard setters to really get at some of the fundamental concepts as building blocks.

I think we have to begin to move in a much more global fashion. I know that may be a little inconsistent with the doable world, but I think we are in a global world and we have to think in terms that we get a set of standards that are going to stand up just as well in the U.S. as they will in China or elsewhere.

So I think there's a huge opportunity for FASB, IASB, and all other standard-setters to really work together on getting to this point of a reasonable set of financial standards and disclosures that support a good understanding of performance.

A sort of second practical one from my perspective is as we think about standards everyone is focused on that there are a number of standards that are very complex, a huge amount of interpretation; 133, 140, ones that affect my space, particularly. But I think in other industries you'd think about other standards, and we should really look at ways of simplifying those standards. I think a very doable action would be to say what are the standards where the rules are the most complex. And we have, I think, some opportunities there to make a difference. Again, using the convergence project may be a good way at getting after that.

I think the third point, and I think that we've heard like we have to get at the underlying system, but it isn't just the standards. It is then going to be the whole process about when is a judgment that somebody makes around the application of a standard and when isn't it, and who has the ability to proliferate, and I use that word judiciously because I think we do proliferate who passes a judgment on how should it be interpreted. Is it an SEC speech? Is it a FASB staff member answering a phone call? Is it a letter that's written?

How does that work? Because at the end of the day, again, wearing my preparer hat that makes life very difficult, and I think probably if we were to spend time on that issue, I think it could really bear a lot of fruit. I understand this is a complex world, that you have to deal with that complexity. However, I am not sure that having again a body of interpretive guidance published by so many different places really helps that. And as a preparer, again, trying to have people say based in Hong Kong comply with U.S. GAAP is difficult when they have to rely on that body of guidance.

The last comment I think I would like to make is just to one that I know and am going to deal with, but obviously, a lot of this is defensive plays around protection on the part of many of the participants in the process around litigation, not something that we can necessarily do something about. But maybe if we don't see this as a conflict between preparers, regulators, and the other participants in the system, and more so where we have a shared goal of doing this better, maybe we can make it a little bit more of a joint effort.

So thank you for the opportunity to give you those comments.

CHAIRMAN POZEN: Thank you, David.

I did want to say one thing. I don't think, since there is the Levitt Committee on auditor liability, we won't be addressing those proposals, but I think legal liability will come up in a number of contexts, and I think we should not shy away from dealing with that. But just the specific proposals for auditor liability, we'll let that Committee run with it.

I would like now to move to Tom Weatherford. Tom serves on the boards of a number of technology-related companies in the West Coast and he was at one point the CFO of another company. And he's here to represent small and mid-size companies. And we're glad to have you, Tom.

MR. WEATHERFORD: Thanks very much.

First, it is an honor to be a part of this Committee. Second, I think that I can basically say and summarize my thoughts very easily. I agree with everything everyone said.

(Laughter.)

MR. WEATHERFORD: It has been consistent, but I think that one of the things that is lost when we look at standards is not only the complexity of the standards, but which companies have the capability inside to actually deal with these standards.

I mean, I receive this every quarter. This is from one of the big four. It's a standard-setter update. It's 24 pages of pronouncements, consensus, staff positions, executive drafts, proposals and reports from the FASB, EITF, ACSEC, SEC, PCAOB, IASB and GASB. It's just very complex, and that's only one quarter's worth of updates. So for small companies, it's overwhelming. A hundred-million-dollar company just does not have the capability of a $10 Billion company, and yet when the standard is created, it's created as though all companies have expertise equally within the corporation.

I also believe, having dealt with international accounting all my life, thirty-two years in finance, five years as a audit committee chair, that the rapid globalization of markets today dictate that we should have one standard. The economic substance of a Chinese company is basically the same as the economic substance of a U.S. company. A French software company has the same issues in terms of revenue recognition as a U.S. software company. They may have better food, but the same challenges on revenue recognition.

Many companies today are on multiple markets. I am on the board of several companies that are on multiple markets in the U.S. and other countries, and they have to deal with one set of accounting standards for that market and another set that can be overwhelming, not only for the company, but the chairman of the audit committee trying to deal with this. So one standard makes a lot of sense. And how we evolved to that: if 100 countries can use IFRS, why can't the U.S. use something like that?

In addition to that, I think that standards need to be simple. When you have preparers trying to understand a standard, auditors trying to interpret the standard, and in today's environment you can't depend on using the auditors like you could in the old days, it's more of a hands-on. So you are left alone. Many times I've had financial analysts call me up when I was a CFO, and after I retired, say, Tom, can you explain what this means, an accounting term, so I can know if this company is cooking the books or not.

So even the users today are confused. So we could have a simple set of rules in plain English so to speak, as we do our MD&A and 10Qs. I think it would help in many ways. I've never used a 10Q to run a company as a CFO, so if you look at a 10Q the way it's structured today, if CFOs don't use it and CEOs do not use it to run a company, how can investors use it to analyze a company and understand the workings of a company. It's become so complex with so much legalese in it and so much repeating of the same thing, page after page, and the risk factors, which if you read the risk factors you wouldn't invest in any company. So there needs to be a simple way for analysts, for investors, whether they're sophisticated or individual investors, to really analyze a company.

In addition to that, whether we have principles or rules-based, the thing that is disappearing is the ability of judgment at the local level. Today, there is more oversight. There is more second-guessing and a lot of it is unintended. A lot of it is perception, but it's there today where the auditors today you can't count on your audit partner to give you a recommendation that will stick. In fact, there's a risk factor floating around silicon valley. It's a joke, that says, we can't guarantee that our results are correct, because our guy in national is too busy to answer our questions to tell us how to do this.

And I think there's some truth in that in the sense that everything seems to go to national today. And I think it's because of the complexity of some of the standards, but it's also because there's the punitive side if an audit partner, especially junior audit partners, get it wrong, even though it's an honest mistake. So we could have a balance there. If we could have a true oversight of these committees, I think that would help. And this is not about cost. This is about giving preparers and auditors the time to really analyze what makes sense. We are taking so much time analyzing pronouncements and standards, which really don't effect the bottom line, that we don't really have time to do the old balance sheet review. And I could give you many examples of that.

So, as a member of this committee, what I would like to do is to try to push towards a simplification, to take every type of organization that's here represented today and have us work together, a way of doing this a lot simpler, because I believe that it is too complex. And, as a result, it's made it even harder for investors and preparers and auditors to do their job properly.

Thank you, Mr. Chairman. Thank you.

CHAIRMAN POZEN: Peter Wallison, who's out of the country, apologizes. He couldn't make it today. He, as many of you know, was General Counsel of the Treasury and has been involved quite extensively in XBRL and interactive data for financial reporting. So he is an expert in that area and will be involved with the Committee.

I do want to give the observers a chance if you want to make a short comment. Bob, I don't know whether you wanted to say something.

This is Bob Herz, Chairman of FASB, and also long-time senior partner in audit firms.

MR. HERZ: Yeah, thank you.

To me this is kind of like a dream come true, because I've been asking for an effort like this for probably the last two years. So, again, I thank not only Bob but I thank each of you. And hearing everything around the table, back on a lot of my own thoughts on the whole system, you know, if I were to go about trying to think about this and how to go about it, I'm big on kind of thinking about things in product development terms.

We have to start from scratch almost and create a product that met the needs of the market, you know, what attributes would it have and how would we go about doing that. Then we'd kind of compare that with the current state and think about what are the constraints on creating this dream product. Now that may be over ambitious, but it may be a way to also kind of frame this to whether or not the recommendations you come up with actually improve the state of the world towards the objectives that everybody seems to be trying to meet.

So I would encourage, although this is kind of a regulated area, to think as a little blank sheet of paper out of the box. My way of doing that is to think about what product or sets of products would we try to market to the market and will they be bought.

CHAIRMAN POZEN: Okay, I think also Mark Olson, the Chairman of PCAOB, I don't know whether you wanted to add a few comments.

MR. OLSON: Bob, just first let me second Bob Herz's comment.

Over a year ago, when I became Chairman of the PCAOB, one of the first visitors I had was Bob Herz, who was suggesting the need for this Committee and was hoping that he could count on the support from the PCAOB. A couple of comments; first of all, I'm glad to hear you talk about focusing as being critical, because as you read the discussion draft, what it leaves out is the enormity of the challenge that you've laid out and the relevance of a limited time frame.

I think Linda was the first one that made the comment about the fact that it's quite a large task. And Nusbaum had said that he can sense just from the comments that he's heard so far that there has been a certain focusing take place. And I think that that's useful, because I think we're going to have to do that first in order to achieve the objective.

A second perspective: most of the talk, appropriately, is focusing on the relevance and the clarity of financial reporting so that it's meaningful to the various audiences based on their needs and on their sophistication, and on their perspective.

But there's another element, too, in the U.S., and we're very proud of the confidence in the markets that we have. And the SEC and the PCAOB were both created by the Congress at a time when that confidence went away. And rather than playing the role of defense, hopefully, if we're doing it right, we're playing the role of referee. So that, when we get questions such as are we second-guessing, we are instead reinterpreting that role. Is the appropriate amount of professional skepticism being applied as opposed to the second-guessing.

So we get it out of sort of the backyard playground amateur approach to a much more sophisticated level of judgment consistent with, you know, what is happening now in the capital markets. But just going around the room listening to the various perspectives, shareholder, issuers, audit firms, analysts, underwriters and now regulators, the symbiotic effect of having that many players involved in this process will almost surely make it somewhat complex. And so I really welcome the opportunity for us to try to sort through that complexity to help achieve our respective goals.

When we were first invited to participate, it was almost like being invited to a party that said, you are invited to a party. What can you bring? Because of what the SEC was asking for was not simply our involvement, but for our staff support. And Greg Skates, who was going to be involved in the process has become familiar with the term, secondment, recently. But in addition to myself, I am very pleased that Charlie Niemeier, one of our other board members, and also Dan Goelzer, who is not here, will be very much involved. We're very pleased to be included in the process and look forward to our involvement from the perspective that I just mentioned.

Thanks, Bob.

CHAIRMAN POZEN: Thank you.

I think Arthur Leder sitting in for Charles Holm from the Fed, did you want to say anything, Arthur?

MR. LEDER: Bob, in the interest of time, I yield my time in order to get us to the next discussion point.

So, I don't have anything to say other than Charlie regrets not being here. He had another commitment and we greatly support the efforts of the SEC and the Committee to improve financial reporting.

CHAIRMAN POZEN: Thank you.

Kristen Jaconi from the U.S. Treasury Department.

MS. JACONI: Well, we want to thank the SEC for including us in this Committee, and in the discussion paper, two Treasury initiatives were mentioned. One of them is a restatement study, and of course Con Hewitt had mentioned the alarmingly high number of restatements in the past decade.

We of course will share the results of that study, probably first quarter of 2008, and then we are also forming an advisory committee to study the sustainability of the auditing profession. That will probably begin in the Fall, and perhaps recommendations released by early Summer. And again we'll share those recommendations with you.

CHAIRMAN POZEN: Thank you. I think John White who's the Director of the Division of Corporation Finance here at the SEC and a very distinguished securities lawyer might want to say a few words.

MR. WHITE: I am very pleased that all of you are here undertaking this job. I guess I just wanted to comment real briefly on the two roles that we play here from the perspective of Corporation Finance. We are the group here at the SEC that actually reviews the financial statements that we are talking about here. But not just the financial statements, but all of the other financial and non-financial disclosures about 4,000 companies a year. And so we are really looking forward to your help and suggestions on that front.

The other role we have is that we are the group that proposes a large number of the new rules to the Commission, and so I guess I am really looking to Joe Grundfest and some of his comments.

We would really appreciate your giving us some things that are practical and useful and that we can realistically propose to the Commission in the time frames we are talking about, and so on, because we are the guys that actually are going to implement this in many cases. And, so, please give us something that we can do in a realistic and practical way.

Thank you.

CONCLUSIONS AND NEXT STEPS

CHAIRMAN POZEN: Thank you.

Let me make an attempt here in the modest amount of time we have left to sort of summarize and get a little discussion on some of the points that have been made here. First, starting with a process issue Joe mentioned to open the tent, and I think the ideas I see coming out of this and just sort of want to run them by the Committee and get some other thoughts on this is the paper that you have in this little booklet, I think we were intending with the

Committee's agreement to put it out for comment in the sense of trying to solicit input as to the scope of the Committee's work. So that was one idea.

A second idea which Joe is talking about is having more of a blog, more of communication, and I think that's a good idea. My main thought about that is that maybe as the work of the Committee progresses and we have some more focused questions that we could do that, I am a little concerned about opening it up too early, because we might get a lot of stuff all over the place. But I do think the idea of using the web site proactively or through blogs and maybe one of the things that I think we can ask the working groups as they go along is for the next public meeting is to try to formulate some sort of request for comment through these blogs that's focused, so we can get that benefit.

A third thing is that the idea here would be to have most of the public meetings open meetings in Washington. But I do think we would like to have a meeting in New York and a meeting in the Midwest and a meeting on the West coast. And so I think we would try to arrange these meetings so that at least part of the time those meetings we could have testimony from people who the Committee felt really had something to offer.

And I think that we need again to make sure we don't just have a gab fest. You know, sometimes I've been at some of these testimonies where they sort of go on and on and on, but if we can figure out, I'd encourage each of the working groups to figure out who in particular they would find to be a very useful person to testify on a focused subject.

I don't think it's really helpful to have somebody give a general view about all the financial system. That's our job. But if somebody, for instance, was a real expert on XBRL and could address some issues that really could be useful for the whole Committee on understanding the implications of that, and I think some of the other things people have said about press releases, and there are a number of topics that could be done. So I think people ought to think about getting participants to testify in sort of a more or less focused way.

The fourth thing, which I guess has come up, Joe probably focused it in terms of what else has been done and is being done, I guess I do think the fact that the Treadway Commission still is remembered. I think the answer is that the Treadway Commission wins the prize for the advisory committee that still is referred to in a number of SEC rule-making proceedings.

MR. LIDDELL: But it wasn't a federal advisory act committee.

CHAIRMAN POZEN: It wasn't a federal advisory act committee. Okay, we were not sure of that. Anyway, it may or may not have come before we were all subject to the wonderful rules of FACA. But it was in the nature of an advisory committee and it did have a big effect. And I think it led to COSO. I think we'll ask the staff. We'll ask Jim and Russ to take a look at other advisory committees to see what they recommended and why it did or did not come about and I think, more broadly, to look at other studies that have been done so that we should at least recreate the wheel and have a good sense in these areas of what other studies have been done.

And I would say as a "C" matter under that, "A" being other advisory committees, "B" other studies. I know that there are some ongoing efforts, that the Center of Audit Quality has held a number of meetings in which they have tried to solicit from investors what are you really interested in. And financial statements I know the AICPA, I think they have some sort of, I don't know if it's a survey or study about what people think when they read the audit opinion, what they think they're getting there.

So I think we should have the benefit of what's been done. That's a chunk of this just in terms of process, so I was going to stop there and ask anyone on the Committee whether they had any other suggestions as to a process basis of things that they would like to see us do.

Well, I think what I've mapped out is actually quite a big program in terms of just getting the background. But I think what we'll do is try to think of some public meetings in some of them in the future as being partly meetings of our own to discuss this, and partly ways to get participants in front of the Committee.

A second thing just somebody raised, and I think it may have been Jeff but I'm not totally sure, about priorities. I think we were trying to say that we have two main groups, the investors and preparers, who are affected by financial reporting. I think, and people should express their view that I think that we would probably agree as a Committee that between those the priority should be on investors. I think this is what Chris may have said, rather than preparers.

On the other hand, I think we ought to recognize that the preparer community has to bear the brunt of some of this. And so if we asked all of Jeff's analysts what they wanted, they would come up with a very long list, since I know we're on portfolio management and analysts. And so we need to be constrained in a practical way of what is reasonable for the preparers to publish.

And third of all, I think we ought to recognize that there are sort of various groups which we think of as intermediaries, auditors on the preparer's side and analysts and people like Motley Fool on the investors side for these have to be run through. So I don't know whether that seems reasonable from the point of view of the Committee in terms of just people want to reach some sort of preliminary viewpoint on that.

I don't know whether Jeff or Chris want to comment on that?

MR. LIDDELL: Yeah, I'm happy to just endorse what you said and repeat what I said. From my point of view, investors are the primary group who we are trying to optimize for here. So in the case of conflict we should be optimizing around them, but with the practical overlay that it has to be done on a cost-benefit basis. Certainly, when I talk to investors, they initially start with a wish list that's as long as your arm. But when you actually come down to the practical suggestions that they have about what they really want to see, it's a much more finite list.

And when they do accept the fact that there are costs involved in getting a longer wish list and they really don't want to have to bear those costs to get the incremental amount of information. So I think investors is the right paradigm to take here, but applied in a very practical sense.

CHAIRMAN POZEN: Jeff?

MR. DIERMEIER: Yeah, I guess I would only add that that makes perfect sense. The financial reports are for the investors. The assumption is that inside the company there is all the information that you possibly could have by definition at the disposal of management. So from that standpoint, management is not in the dark in terms of what information might be available.

So from that standpoint, I think it gets a slight priority edge to the end users in terms of financial reporting so to speak. But your comment about, you know, obviously there has to be a check balance there in terms of what the preparers can actually come up with in a cost-effective basis is pretty critical.

CHAIRMAN POZEN: Yes, Denny?

MR. BERESFORD: There's one constituency that isn't represented here that has a great interest, and that's the academic constituency. I guess Joe and I--

MR. POZEN: Some lawyer is going to have to tell us whether a legitimate constituency for the purposes of this, we were told, you know, in this theology that we're not sure whether they represent it. But, we'll be glad to have you double in that role.

MR. BERESFORD: I apologize to the act or whatever it should be, but my point is that I certainly agree with the idea of the privacy of the interest of the investors. And of course, Chris made the point of cost benefit. I think we also have to take into consideration the doability of some of the things that we're talking about here. I'm thinking in terms of educating students. I think that maybe we haven't kept up to date with some of the things that we should be doing, but to be very honest, the complexity of the accounting model is beyond even the masters of accounting, specialist-type students, these days.

I met yesterday at FNMA with a couple of people who spent full time, they're very senior people in the organization in the accounting area, they spend full time on securitization transactions. They have 20 people in the accounting policy area to try to make sure that they cross all the t's and dot all the i's and so forth. So I think that we just have to take into consideration the practicality of many of these issues. It might be nice to do some additional things, but sometimes they're beyond our human abilities.

CHAIRMAN POZEN: I think your point is very well taken and I don't know whether anyone else wanted to comment in this area.

MR. COOK: A comment just supporting Denny's view and also encouraging maybe in responding to John's comment about give us things that are practical and actionable and so on. I don't know what is actionable and practical, but there has to be some understanding on our part what kind of flexibility might be there. I harken back to the mid-1980s.

There was a lot of time spent by the firm and by the SEC and by FEI on the concept of summary reporting, and substituting a summary report, a condensed version in plain English for the extensive compliance type disclosures, and it never really took off.

An interesting anecdote was offered by the CEO of one company in opposition or in contrast with the product of the company that made cookies. And they offered a box of cookies or the annual report. Take your pick. And 93% of the people voted for the cookies, because they said, we'll eat the cookies, and we don't get any value out of the annual report.

So we were trying at that time, just to make this point, trying to find a way to substitute a communication that would be useful for a communication that was not receiving any marketplace acceptance. And it never went anywhere, because we couldn't get beyond the point of everything else would have to be provided the way it had always been provided, and this would just be an add on. And companies said, gee, it's a good idea, but I don't want to pay for an add on. And so it died in the mid-'80s, late-80s, despite being a concept that seemed to have a lot of value.

What can we learn about the ability to implement ideas about streamlining communication processes and so on, so we don't just make a recommendation. Somebody says, that's nice, but sorry. We can't do that because we've got 17 reasons why that won't work.

What's out there John?

MR. WHITE: Well, one thing you might want to look at, I know we have not been saying nice things about past FACAs. But the Small Public Company Advisory Committee, which presented their report in April of last year, we did put forth, and I think they had like 25 recommendations separate from their 404 recommendations. But this May, which would be I guess 13 months later, we have just recommended to the Commission, and they have put out I think about seven or eight hundred pages of proposals off of their recommendations.

And what you'll see is we just kind of picked pieces of their recommendations that we thought were realistic that could be done in an effective and a practical way. I mean, that's at least an example of where we had a recent committee who's given us a lot of recommendations, and at least as a first wave we tried to pick what we think we can do out of it.

But those haven't been adopted yet. I mean, obviously, those proposals have just come out.

CHAIRMAN POZEN: And have flexibility to look at them.

MR. WHITE: Yeah, I mean, that's just an example of seeing where you really have a good one.

CHAIRMAN POZEN: That's good, very good. Bob?

MR. HERZ: I echo Mike's comments, because in my former incarnation, probably 7 or 8 years ago, I actually chaired a group to look at integrating and streamlining the whole financial reporting package, and SEC GAAP redundancies, and that. And we started to take a kind of a nascent look at technology and the possible things like click-downs and tiering of information.

And one of the barriers at that point was that the difference between the legal regulations around what was in financial statements, audited versus MD&A versus other, started to create at that time was called "in the envelope, out of the envelope" kinds of issues. And we were told that's going to be difficult to modify. So if we're going to really look at this tiering of information issue and summary information, all of those kinds of things that are now cloaked in the regalia of different forms of legal protection and liability, I think there needs to be flexibility in that, I think, just thinking down the line, if we're going to think about those kinds of potential solutions.

CHAIRMAN POZEN: Well, that's a good segue. I was going to try to summarize in each of these four areas sort of some of what I had heard, and just if I didn't hear it correctly, people should feel free to come in. And so picking up on this whole area of information delivery, I think I heard some very important points about wanting to allow summaries, and I think the point that Bob Herz just made is the critical point. Whether it's the summary or it's a selective array of information that's, you know, sort of a business indicator for a particular industry, one of the key questions is going to have to be the liability issues; that a lot of the willingness of issuers and registrants to do this, by its very nature, the investor is getting a partial.

And there has to be some notion that if the investor, whether it's through hyperlink or getting a full prospectus or full annual report, that they will be deemed to have gotten the full document. Because otherwise people can be very afraid to have these essentially subsets of information. And I think that's the key question that that group is going to have to look at. Another key question which I think a number of people have read is that XBRL has a lot of potential. The difference between potential and realization is huge, and I think that as Susan points out that in the banking area, it's been very successful. It's an easier environment to work in, but I think there is something really to be learned from that.

Some of the things that people want from XBRL are more standardized to the extent for instance you could have industry performance indicators that were agreed upon by an industry, but to some degree, you have real customization where the analyst community wants a degree of customization that, you know, would provide some real challenges in terms of how that's done.

I think I heard two other things in this whole area. One is the importance of the MD&A and sort of trying to, if anything, expand that and give people more comfort, give the writers more comfort that they can be expansive and they are sort of free-writing. And I am sort of interested, John, about your experiments at free-writing in the 33 Act area where you've been allowing people to deviate a little from the standard sort of language in these prospectuses.

So I think that that's an area -- both MD&A and the free-writing, which is something that's now allowed in the 33 Act process where before it was highly stylized -- free-writing might be viewed as allowing in writing what people used to say on road shows. But maybe that's too cynical a view.

And I think a fourth thing which quite a few people have mentioned is we have a lot to learn from the press release. We have a lot to learn from the earnings release. We need to make that a central part of our inquiry, because the press release represents sort of what the companies and the analysts are jointly thinking of. This is what's really important; and, you know, you're stripping out, whether it be stripping out one-time events or stripping out currency fluctuations into some sort of concept of core earnings, however it's defined, and then these other things.

So those were four things that I heard in the information delivery area, though I believe that the press release, also, I think, has implications for the substantive complexity group.

But I am going to just stop there, and take people's comments on that.

Yes, Greg?

MR. JONAS: Bob, just first I'd like to echo I think that's an excellent summary of the display here at the delivery part of the program.

Your comments about MD&A are particularly relevant to me as I think of the many, as I mentioned before, meetings that companies come to give us updates on their business and the huge contrast between a face-to-face discussion with management versus what we read in MD&A. And typically in the face-to-face meeting, management delivers a book that are pictures, graphs and charts. And what management does is then put their color around those graphs and charts, and it's wonderfully clear. It's really insightful. A lot of the things in the graphs and charts don't have dollar signs in front of them, a lot of non-financial data. But it's just the marked contrast between the clarity of the face-to-face meetings with the pictures versus what we see in MD&A, and hopefully we can get some of that clarity into that reporting process.

CHAIRMAN POZEN: That's very good.

Anyone else want to add something?

MR. DIERMEIER: Bob, if I could add something, because I think maybe your first point on all summaries, maybe you were trying to get to the smaller, the less sophisticated, the serious investment amateur so to speak. But it seems like there seems to be some focus on that element as opposed to just the professional investor.

And as I try to think about this, the only way I can see getting at that is literally, I think, there may be questions about segmenting these individual investors in terms of what they try to get out of the financial statements, what they're doing. Many individual small investors are not trying to pick a stock the same way we might do it in the institutional world. Their portfolio might be dominated by single stocks they wouldn't allot, or it might be that they're just trying to get exposure to an area of the marketplace.

So, I think it might be helpful for these individual investors in these reportings to actually think about the segments themselves that they come from, because that might inform our discussion.

MR. GRUNDFEST: Greg, with regard to your observation about how the information you get in these face-to-face meetings is typically infinitely more valuable than reading a 'K' or a 'Q' or a press release is exactly right, and we have to understand two reasons why that's the case.

Number one, a lot of the information you get, companies wouldn't want to have disclosed to their competitors. All right, so we have to understand that in every situation when we're talking about disclosure here, one of the other balances is anything you put in your 'Q' your competitors are going to read. All right, you know, people go through the exhibits to S-1s in Silicon Valley, you know, a little bit like they're the hottest, steaming novel that you'll ever see.

Because the information that's required to be disclosed has real competitive value, and a lot of companies don't like going through the S-1 process, because they say, look at everything we have to disclose to all of our competitors. It's going to be a road map for how we're doing our business, then you compete with us. So, you know, understand there's a little bit of yin and yang in this.

And then second you've got the litigation environment. It is relatively easy to sit with you and talk about metrics that don't have dollar signs associated, because you understand how those translate to dollar signs.

If I am going to do the same slide show and try to explain all of the stuff in a way that I can feel comfortable that I'm not later going to be sued in hindsight with regard to the information I'm describing, I'm not going to present the same information the same way. So that would suggest we need to think potentially about broader safe harbors for certain types of disclosures if we hope to call them forth.

CHAIRMAN POZEN: Well, I think that's a well-taken statement and it leads us into the third area, the compliance audit area, where I think legal liability is there. And it's there both in terms of class actions and it's there in terms of SEC enforcement.

And I think that while we're not going to be proposing something for auditors, I think we need to think through that. I also heard a number of people refer to restatements, and we will take advantage of the Treasury study of restatements and understand that.

A third thing I heard is Linda is making good example of revenue recognition, which may be a good case study in terms of trying to understand how people get themselves into trouble and why and whether there's anything we can do about that.

The fourth thing, which I think in many ways the most important but the most difficult is there are quite a few people who use the phrase second guessing, and I think everyone is concerned about second guessing and I think it relates partly to what I call the judgment element of principles versus rules, because I guess Mark if I were to say that the one thing that comes out of AS-5 now is that the auditors should use more judgment, but if the auditors use more judgment and then somebody comes in and second-guesses them, then they are going to feel like they're just being set up.

And I think one of the tasks of this Committee in that particular work group and a very challenging task is to try to understand how it is that we build a system that encourages judgment from auditors. But obviously, PCAOB can't be in the position of just saying, okay, you exercise judgment, you're automatically right. On the other hand, there's got to be a degree of discretion there. There's got to be some ability to make choices, and I think that's one of the things where, you know, that we'll really have to grapple with.

We look forward to a full and free discussion on that point. I guess all we can say is the exercise of judgment of auditors is now elevated to a new level. Everyone's in favor of that until someone gets zinged in an inspection. I don't know whether a lender or anyone else wanted to say anything else about this third area of compliance and audit.

MS. GRIGGS: Well, I guess someone else mentioned materiality as being one of the issues that may be necessary to grapple with in dealing with restatements. I know a lot of our clients have restated for reasons that may not be material to a sophisticated investor, but that's a hard judgment to make. And so, is there a way to try to come to grips with making those judgments, which cash flow statements, which is my particular bugaboo, don't need to be restated, even though somebody classified amounts incorrect.

CHAIRMAN POZEN: Well, I think that's an excellent point and Greg may be able to help us, because I think Moody's and a lot of other people look at a lot of these restatements and maybe put out a report sometimes; make a judgment.

Because there are so many technical restatements (I don't know what the right term is) and try to understand what restatements are really making major financial changes versus ones that seem to be of a more technical nature.

MR. JONAS: You know, Bob, I think in a nutshell it's entirely possible that amounts could be very large and error could be very large and the market wouldn't care. That happens, for example, when the amount happens to not hit metrics the market believes are the drivers of value.

CHAIRMAN POZEN: And I think a number of us have been in situations where we've had to restate where the ultimate bottom line wasn't actually changed, as you say, but some aspect of how you got there changed, and timing and these sorts of things.

So I guess one way to look at this is we might want to understand which situations the market reacts to as they are telling you something about the significance. And the other thing that I think is involved with that is trying to figure out other ways to deal intelligently with the mistakes. I mean, because it's not that we're trying to make believe that there weren't mistakes or perhaps maybe in certain things, it's not so much mistakes, but sort of new understandings of certain accounting principles, whether it is a way to deal with that prospectively rather than have this enormous number of retroactive. At least in my mind, I think, one of the measures of success of this Committee is if five years later the number of restatements has been reduced because we've given people better guidance and we've also defined what are the really important things that change versus not.

Just to try to summarize going backwards, is the areas of rule making and standard process. I think we heard a number of people basically saying in one form or another there's too much GAAP parading around. Obviously, what FASB does in a very succinct and quick manner is GAAP.

But as somebody said, if you ask your audit firm what's GAAP, you get this long essay and it includes something that somebody gleaned from an SEC comment letter and because they dealt with it in an enforcement proceeding, something happened, and then maybe even something that accounting fellow said in a speech or something that came up through EITF, so I think that we need to have a much more disciplined process, and I know Bob Herz agrees with this. We surely don't want to stop lots of people from interpreting, commenting, kibitzing, whatever way you want to say it, but we need a better sense of what actually is GAAP. And then it's almost like everything else should have a stamp on it. This is not GAAP, this is our views. You know this, so you can have auditing firms or organizations that put out guides or their views.

I think we have to be a lot clearer distinguishing what's GAAP from what's not GAAP, and people have done these things. And I think the other thing you hear is because FASB takes so long and comes out with these standards that are quite complex, that the reason this is happening is because people are seeking guidance, that they can't find it in these long statements, and they also want it in a more timely manner.

And I think that both Con and John are providing on a registrant basis some ability to deal with that. Now, people may fear that and that's something we ought to explore, but I think there are ways through your processes to get reactions on a registrant basis about whether this particular way of accounting makes sense. I think the bigger problem that we need to grapple with is the sort of what I call intermediate level issues, which aren't registrant specific. But they are not global, but they are sort of areas as people think through these statements where maybe you get a whole new type of derivative that comes up or you get a whole area that people just haven't thought about being within FAS 140, and now people are thinking of it as FAS 140.

So those are areas, and I don't know whether its through the EITF or through rule-making proceedings or other things, so it seems like that's an area where the Committee could on the one hand get a much more disciplined and narrow definition of GAAP. And, on the other hand, get a sort of more enunciated and articulated way for people to get guidance faster at different levels. So that's what I heard in a variety of different forms. I would be glad to take anyone's comments on that.

Susan?

MS. BIES: I want to second the comments that you're making. And I think one of the projects that I know Bob's group is working on is this codification, and I think that's essential. I mean, there needs to be. It's getting so complex and so many projects and there have in the past been too many accounting rule setters. We need to find a way that someone who is trying to figure out what is the way to look at the accounting treatment for a transaction to go to it.

Right now, you have to go through it by standard, and I think it's importance in the staff speeches for the SEC and all the things people have said. I think also as you just mentioned is a lot of this comes into confusion because of the innovation. There's new kinds of products, there's new service streams of building business revenue. They also create gray areas and what old accounting can apply to new innovations. And until that gets settled through a rule-making process, someone has to account for it.

So I think there needs to be a way and maybe through something that is out of the codification project or something like that that helps people focus on what are the relevant issues they ought to apply to a transaction that may be innovative.

CHAIRMAN POZEN: Okay, thank you. And then, yes, Denny?

MR. BERESFORD: Just one other small point. I am reminded by it sitting next to Sue.

I think that one issue that hasn't been mentioned is what I would call regulator GAAP, that particularly in the loan loss provision in banks, I think we've had for a long time a disconnect between what the bank regulators insist on and their version of GAAP versus what the FASB thinks should be the case.

We talked around this for a long time, but that's one specific example. I think there are other cases that the regulators basically say you shouldn't follow anything other than GAAP, but it's their version of GAAP.

MR. COOK: Bob, could I ask a question on this -- I don't know quite where this fits, but it sounded familiar as we were talking about too many GAAPs and too many rules. The question, and I just don't know the full scope of the codification project, but who will consider or where will we consider the issue of sunrise/sunset -- taking a look at these standards -- taking a look at things that have been there. The point Greg made -- we've been adding things on for 40 years, but we rarely if ever take things away. So we have segment information. We just by rote keep producing this segment information and for many people they say it really isn't useful. Then when they do go to their earnings release they put out segment information -- revenue segmentation -- that is very useful, that is never produced in their GAAP financial statements. They are still cranking out these capital expenditures by this and by that.

Bob, does this bring -- does this come up in the codification? Do we look to see if --

CHAIRMAN POZEN: I think it is listed within the standard setting working group that how to deal with existing standards, subsetting is listed within that group for working purposes.

MR. HERZ: I think there's two issues here. The codification is just to put all these multiple forms of GAAP in an integrated form. It won't read like a novel but it will all be in one place by topic so you don't have to figure out where it was.

And the SEC guidance that they believe is mandatory will be in a separate section by topic so it may force some discipline on them because they will be contributing to the codification as well. Anything that's not in the codification will not be GAAP, and therefore will only be one level of GAAP at that, what is in the codification.

The second issue, I think is really an issue of our processes, our agenda as to whether or not you think whether we go through and do things, setting agenda properly looks at the efficacy, cost effectiveness of existing standards on a timely basis or not. And I very much welcome that kind of input.

MR. COOK: I was thinking, Bob, and I think that would be helpful, but I wasn't thinking just about an individual standard but information content which adds to complexity just by volume. Segment information, what I refer to the statement of comprehensive income, which is incomprehensible to most people. What would make that statement go away if nobody found it useful and yet it is part of the complexity because people are producing it? I was looking for --

CHAIRMAN POZEN: I think we're not going to ask Bob to give you the definitive answer but I do think --

MR. COOK: No, no. I wasn't looking for that. I was just asking where are we going to look at the question.

CHAIRMAN POZEN: I think we will look at the question of sunsetting and grandfathering and these things in the working group on standard setting.

John.

MR. WHITE: A couple of random comments. One, the smaller business advisory committee recommended to us that we eliminate all the small business forms, hundreds of pages of forms. That's one of the recommendations that we have put before the whole system, to just change the whole system, to get rid of a ton of stuff.

A couple of other thoughts that came to me. In terms of the timing of your recommendations, I mean I'm looking at some of the things we're thinking about doing. We're moving, for example, on XBRL and future XBRL rule making. we're going to be doing stuff before next August is my guess and so if you wait until a year from now to give us suggestions that's going to be behind the curve that we're operating on. So you should not lose track of making the interim recommendations.

Again, you'll see that the other advisory committee I'm referring to made some interim recommendations that we accepted. And so just to put that in your toolbox, I would think you probably should think about that.

CHAIRMAN POZEN: Well, we do -- I think one of the people you may not have realized that's been seconded to be a staffer on that group is someone from your group, so hopefully that will help us get into the -- time frame.

MR. WHITE: Really?

CHAIRMAN POZEN: I did want to mention that.

MR. WHITE: You should have mentioned that.

I guess just a couple of other, again, random thoughts for you to think about. I guess when I started 15 months ago there were -- we had posted 500 sets of comment letters. We have now posted something like 10,000 sets of comment letters. We thought we were doing a good thing from a transparency standpoint but I kind of listened to this and I -- maybe you should think about what it means to have -- because we literally have put up -- most of those comment letters have come up in a little less than a year.

CHAIRMAN POZEN: I guess we need to think about the difference between soliciting comments and compiling summaries versus just having all those raw comments out there. That's a good point.

MR. WHITE: I mean one of the things that we have thought about where we're doing targeted comments like on the new executive comp rules, we're doing a specific review project there where we're looking at hundreds of companies, we have actually held up putting out any comment letters until we have looked at a large number of companies, we've gone through a first review, we've learned how we think the comments ought to work and now we're going back and relooking at all those letters before we put out any of them in hopes of having some consistency in the comments when we do put them out.

But I mean there are some possibilities.

CHAIRMAN POZEN: No, those are very useful suggestions.

MR. WHITE: The final one, on the liability front, I think we are open to figuring out ways to at least try to work with you and I'll just say, phase things in. I mean in the XBRL area where we certainly are focusing on, in the voluntary program, that information is coming in not the normal liability way. In the 404 area where we have for all the smaller companies the management report coming in in the first year and the audit report coming in in the second year, those management reports are always coming in in a furnished way instead of filed, just in a phase in way from a liability standpoint, just to throw out some more possibilities that I -- and we are great believers in incorporation by reference, by the way. So I mean I think -- you give us some recommendations like that I think we --

CHAIRMAN POZEN: Good. That's great.

In the interest of time here, just the last area, the substantive complexity area. I guess that' the area where we heard a lot of genuine and I think well founded criticism of complexity, not so clear exactly how you solve that problem.

I think people are pointing out that on the other hand economic transactions are more complex, and there are differences between users and preparers. I guess my sense is that that committee might -- there have been a number of, I think, useful points. Maybe one way is approach this area by looking in depth at a few examples.

I think Denny mentioned business combinations as an area where -- unclear whether that's becoming complex unnecessarily, the fudge being in unnecessarily.

I think Linda mentioned 159. 159 is an alternative standard for using mark-to-market or historic in certain circumstances and how that turned out. Did that just produce more complexity by allowing people to have alternatives and then people then fought about whether the alternatives were being stated in accordance with the principles?

And I think obviously hedge accounting is another area. The last thing I would say here and then another comment is I think that Joe makes an interesting point about whether there are areas where we're assuming or we're sort of making believe like there's one simple point when it's really a distribution of probabilities.

MR. GRUNDFEST: Let me go to that for a moment because complexity is not always a bad thing because sometimes if you're going to honestly describe a complicated transaction you have to give a complicated answer, and its foolish to expect that everybody is going to be able to understand a complicated, honest answer. And by forcing somebody to give a simple yes/no answer to a complicated question, you can be forcing somebody to lie. I don't think that's where we want to go.

So complexity is not necessarily the enemy. I think what we have to look for -- look, when complexity is used to obscure, when complexity is used to evade, well, then you know it's a variant on fraud, and that's a very bad thing. But sometimes we try to derive simplicity in such a way that it really gets in the way of comprehension, all right, and we shouldn't do that.

Very simple point, you know, the army of 20 people, you know, trying to figure out how to do securitizations -- well, you could probably fire half of them, all right, or have them do higher valued things for society like revenue recognition, I don't know. You could reassign them to do other things if instead of saying, you know, we had to put this transaction in one pigeonhole and one pigeonhole only, if instead we could say, you know, we can look at this transaction and fairly characterize it one way, a, b, or, c, for the following reasons, and then let's just explain that to the world. It has a variety of different characteristics, all right, and let's explain that honestly. You try to force this characterization into one pigeonhole you're going to make us all nuts and its never going to fit in there in a very comfortable way, and then we've got to document the reason why we put it in and then we've got a team of 20 people.

So this sense of false precision, this sense of false certainty I think is an enemy to the process and there's a level at which people in the audit profession and the standards setting profession I think have a hard time letting go. Maybe sometimes things are black and white all right, and not all black and not all white, and we need ways to describe that.

CHAIRMAN POZEN: Well, I think that's probably a good summary of our challenges in dealing with complexity.

We all are against unnecessary or undue complexity, but on the other hand it may be the case that in other areas in order to accurately reflect the substance of what's going on we need more sensitivity analysis or more pro rata approach, I mean things that sort of reflect that these aren't all or nothing.

I think -- this will prove to be a very difficult area, but I think that this is something we might approach by looking at specific examples and understanding them because I'm not sure that abstract discussions in this area really get us that far.

And I'd just say one more thing, which I think is in 159, this more general problem of what's mark to market and historical cost is another area where we really have to look closely at how we can do that better. Again, a very difficult area.

So I think that we surely have a brief that's broad enough. And I think back to what Joe was saying, I think we will try to make ourselves famous as an advisory committee by coming up with a small number of proposals that are doable. We intend to work closely with John and Con to try to make sure that this isn't just done at the very end. But we'll understand where your processes are and try to make this as useful a group as possible.

So I think we've run a little over time but I think -- if anyone else wanted to say anything? So then why don't -- we're going to close at this point. Jim, I don't know whether you have to bless us to close.

MR. KROEKER: I think Bob, committee members, observers, thank you very much and the meeting is adjourned.

CHAIRMAN POZEN: Thank you, very much.

(The meeting was concluded at 11:50 a.m.)

CERTIFICATION

I hereby certify the accuracy of this record of the proceedings of the SEC Advisory Committee on Improvements to Financial Reporting.

Robert C. Pozen
Committee Chair

Date 9/19/07

EXHIBIT A

Open Meeting of the
SEC Advisory Committee on Improvements to Financial Reporting

Auditorium, Room L002, SEC Headquarters
Washington, D.C.

Thursday, August 2, 2007, Beginning at 10:00 A.M.

AGENDA

I. SEC Chairman Welcome and Introductory Remarks

II. Additional Opening Remarks and Introductions

   a. Conrad W. Hewitt, Chief Accountant

   b. Robert Pozen, Committee Chair

III. Presentation of Discussion Paper

IV. Comments on Discussion Paper

V. Conclusions and Next Steps

VI. Adjourn (expected no later than 1 P.M.)

EXHIBIT B

Discussion Paper for Consideration by the SEC Advisory Committee on Improvements to Financial Reporting

By Committee Chair Robert Pozen[1]

Draft dated July 31, 2007

Introduction

This white paper is provided as an outline for consideration and discussion by the Securities and Exchange Commission's Advisory Committee on Improvements to Financial Reporting (CIFiR). The purpose of the document is to provide a working outline, including a discussion of issues, views and potential consideration points that the Committee could evaluate. Additionally, the outline is structured in 5 key areas that could serve as a model for organizing the work of the Committee into subcommittees.

Background

The U.S. capital markets are the deepest and most liquid in the world. The acknowledged success of the U.S. capital markets, and their contribution to the nation's economic vitality, has been due in no small measure to the availability of relevant, reliable, readily understandable, and timely financial information. However, while the U.S. financial reporting system has become the most complete and well developed in the world, some parts of the system may not be fully aligned with changes in the economy, business operations, technology and investor needs, leaving room for improvement.

The strength of the U.S. financial reporting system lies in no small part in its inherent checks and balances, including the different perspectives of participants in the markets — direct participants (e.g., companies and investors), regulators, independent standard setters, and other third parties (e.g., attorneys, accountants and auditors). But these different and sometimes conflicting perspectives have contributed to some of the problems in the system, including its extreme complexity and the resulting need to consider how the usefulness of reported financial information can be improved.

The SEC has charged the Committee with examining the U.S. financial reporting system to identify ways to improve the system of financial reporting. In considering this mandate, the Committee will consider ways to both reduce unnecessary complexity and make information more useful and understandable for investors. More specifically, the Committee's charter identifies the following as areas of inquiry for the Committee:

- The current approach to setting financial accounting and reporting standards, including (a) the principles-based vs. rules-based standards, (b) the inclusion within standards of exceptions, bright lines, and safe harbors, and (c) the process for providing timely guidance on implementation issues and emerging issues;

[1] This draft discussion paper was prepared by Committee Chair Robert Pozen. It does not necessarily reflect any position or regulatory agenda of the Commission or its staff.

- The current process of regulating compliance with accounting and reporting standards;

- The current system for delivering financial information to investors and accessing that information;

- Other environmental factors that drive unnecessary complexity, including the possibility of being second-guessed, the structuring of transactions to achieve an accounting result, and whether there is a hesitance by professionals to exercise professional judgment in the absence of detailed rules;

- Whether there are current accounting and reporting standards that do not result in useful information to investors, or impose costs that outweigh the resulting benefits; and

- Whether the growing use of international accounting standards has an impact on the relevant issues relating to complexity of U.S. accounting and reporting standards and the usefulness of the U.S. financial reporting system.

As the Committee proceeds with its evaluation, it may wish to consider the financial reporting system in light of the needs of two primary groups – those who prepare the financial information and those who use the information – while taking into account the overall environmental impact of two secondary groups – those who opine on the information being presented and those who regulate our financial reporting system.

Those who prepare financial information generally want:

- Clear instructions on what subjects to cover in financial reports;
- Not to be later second guessed by regulators, litigants, etc. in situations where reasonable/good faith judgments were made;
- Financial reports to reflect the economic realities of the business, with enough flexibility to reflect the special situation of both the company and the industry;
- To reduce period-to-period volatility of earnings to the extent feasible (for example, in situations where the volatility is driven by changes in estimates but where such volatility has not resulted in a “realized” gain or loss); and
- To prepare required financial information at a reasonable cost, in terms of dollars and management time.

Those who are users of financial information generally want:

- To understand the financial reports, at the level of detail that is desired by each type of user;
- To be able to rely on the integrity of the financial reports (and not be told later they were incomplete, misleading or actually wrong);
- The financial reports to reflect the economic substance of the business, regardless of technical rules;

- Financial reports to reflect, to the extent feasible, actual changes in market values from period to period; and
- The reports to be delivered in a format that makes it easy to compare one company to another.

Those who opine on the specific financial information presented generally want:

- Clear instructions on what subjects to cover in financial reports;
- Not to be later second guessed by regulators, litigants, etc. in situations where reasonable/good faith judgments were made;
- The financial reports to reflect the economic substance of the business; and
- To make a reasonable profit opining on financial information at a reasonable cost.

Those who regulate the system generally want:

- A financial reporting system that provides protection to investors, promotes market efficiency and facilitates capital formation
- Clear instructions on what subjects to cover in financial reports;
- To be able to rely on the integrity of the financial reports;
- The financial reports to reflect the economic substance of the business; and
- All of the above to be accomplished at a reasonable cost to society in relation to the benefits to be achieved.

While the list of objectives above is only illustrative and certainly not all inclusive, one can observe that the objectives of those involved in our financial reporting system are consistent in many respects. All participants want clear guidelines that allow financial reports to be prepared and presented in a straightforward fashion, do not want financial reports to be subsequently deemed to be incorrect, want the financial reports to reflect the economic substance of the business, and do not want companies to spend too much money and management time on preparing financial reports.

However, the Committee should recognize that some of the goals of participants within our financial reporting system may conflict. For example, preparers often want less volatility in earnings implying less fair value measures, while users generally prefer that more assets and liability reflect their current values. This places tension on the desire to have financial reports that reflect the economic substance of the entity. Further, users may prefer a uniform format that makes comparisons easy, while preparers may want special rules that allow them to present what they believe are the unique aspects of their industry or company.

Upon conclusion of the Committee's work, the Committee will provide written recommendations to the Chairman of the SEC on how to improve the financial reporting system in the U.S. These recommendations may cover many aspects of the financial reporting system for the Commission to consider, including recommendations that involve the Financial Accounting Standards Board (FASB), the Public Company

Accounting Oversight Board (PCAOB), and other appropriate organizations. In order to facilitate the Committee in forming these recommendations, the Committee will create subcommittees. The subcommittees will report their recommendations and advice to the Committee for full discussion and deliberation. The proposed subcommittees are listed below. Follow that listing of proposed subcommittees is a proposal regarding their objectives and some preliminary topics the subcommittees may wish to consider.

I. Substantive Complexity
II. Standard Setting Process
III. Audit Process and Compliance
IV. Delivering Financial Information
V. International Coordination

I. Substantive Complexity
This subcommittee will study the causes and impact of complexity on financial accounting and reporting standards, including: (1) principles-based vs. rules-based standards; (2) inclusion within standards of exceptions, bright lines and safe harbors; and (3) the concerns of fair value measurement attributes and related earnings volatility. This subcommittee may wish to consider the following:

Principles-Based Standards
Some commentators have suggested that the US should adopt more principles than detailed rules as a way to reduce complexity. However, other commentators have argued that both preparers and users may prefer bright line rules to avoid second guessing in the U.S. regulatory and litigation environment. In considering the need for principles and rules, the subcommittee may wish to evaluate the recent efforts of the FASB to move to a more principles-based approach while retaining implementation guidance. As a reference point, the subcommittee may wish to begin with the SEC staff's 2003 report to Congress mandated by the Sarbanes-Oxley Act of 2002 on a principles-based approach to standard setting in the U.S., and the FASB's related response.

Competing Principles
Complexity may be created not by the adoption of principles versus rules, but rather as a result of competing principles. For example, U.S. GAAP is not consistent on the appropriate measurement attribute to use for valuing financial assets and liabilities. In areas like financial assets and liabilities, there are two basic principles: lower of cost or market, and fair value. The appropriate method to use in U.S. GAAP may be based on a specific industry, a specific transaction, a registrant expectation, or a registrant choice. To many it would be less complex to choose one approach, but many disagree which approach is most appropriate considering both relevance and reliability. More and more compromises are made, and these compromises lead to greater complexity as lines are drawn or judgments are made to delineate when one approach applies and the other does not. This subcommittee may wish to consider to what extent mixed measurement attributes (fair value versus historical cost) have increased complexity and

reduced transparency, and what changes should be made within our capital markets to allow for more consistent measurement attributes.

Preparers vs. Users
Complexity also may result from conflicts between the objectives of preparers and users. From the perspective of sophisticated users, financial reports would be more useful if they contained more segment information in multi-line businesses. However, most companies are reluctant to have more reporting segments because this may involve the disclosure of competitively sensitive information. This subcommittee may wish to consider whether enhanced information would improve the usefulness of financial reporting in our capital markets.

Industry Specific Exceptions
Many industries have successfully obtained special treatment or exemptions from general accounting standards from the FASB or the SEC. While such exemptions or special treatment increase complexity, they, in many cases, may help preparers within these industries present their financial reports in ways that, in their view, better reflect the economic substance of their businesses than the general standards. This subcommittee may wish to consider whether industry specific accounting or disclosure is useful to our capital markets.

Alternative Accounting Policies
Currently, GAAP allows for entities to elect alternative accounting treatment for various transactions that may be economically similar. Most recently, the FASB issued SFAS 159, Fair Value Option, that allows companies to irrevocably elect to record certain types of assets and liabilities at fair value. This election is an instrument by instrument election. Other explicit options are currently present in U.S. GAAP. Providing companies with options may be a useful compromise when there are acceptable alternatives, but it makes it more difficult for users to compare companies. The subcommittee may wish to consider whether alternative accounting policies are useful to our capital markets.

Sensitivity Analysis
Financial reports are currently presented in a way that may over-simplify an issue with a complex range of results. In certain areas of accounting, the assumptions drive the results – for example, accounting for unfunded liabilities of defined benefit funds. Yet the range of permissible assumptions – for example, discount rates and mortality experience – is quite large. While sensitivity analyses are utilized to some degree, the subcommittee may wish to consider whether further sensitivity analyses would reduce complexity.

II. Standard Setting Process

This subcommittee will study the standard setting process and may wish to consider the following:

U.S. GAAP Hierarchy

Presently, all U.S. public companies must follow U.S. GAAP to be in compliance with applicable securities laws and regulations. Over the years, U.S. GAAP has been developed by many different recognized and unrecognized organizations. In the most recent past, these recognized organizations have included the SEC, the FASB, the Emerging Issues Task Force (EITF), and the American Institute of Certified Public Accountants (AICPA) Accounting Standards Executive Committee (AcSEC). For public companies, the authority to set GAAP resides with the SEC. The SEC has historically looked to private sector bodies to provide standards for financial reporting by public companies, and since 1973 the FASB has been recognized by the Commission for this role, absent any contrary determination by the Commission. In addition, the SEC at times will develop interpretive application and disclosure guidance for public companies. The FASB also allows for the EITF, which is subject to its own oversight by the FASB and the SEC, to develop interpretive application guidance to existing U.S. GAAP.

The FASB has undertaken a significant project to develop a comprehensive and integrated codification of all existing accounting literature organized by subject matter that would become an easily retrievable single source for all of U.S. GAAP. This project may provide a useful roadmap for identifying those areas in U.S. GAAP that could be simplified.

Characteristics of the FASB

Currently in the U.S., accounting standards for public companies are established by the FASB, absent any contrary determination by the Commission, and the FASB is subject to oversight by the SEC. The Board consists of three members from public accounting, two from preparers, one from academia, and one user. While each member of the Board brings different experiences and perspectives, they are selected based on their expertise in financial reporting and are expected to make decisions based on what they believe will improve financial reporting rather than representing any one constituent group. All members of the Board must sever all ties and remain independent. The subcommittee may wish to consider the characteristics of Board members and the Board selection process.

FASB Standard Setting Process

The FASB has an open due process through which the Board obtains input from many constituents, issues proposals and receives extensive further input in the format of comment letters and holds public meetings with constituents. The Board makes all decisions on its accounting standards in public through open debate prior to reaching conclusion. This process can take many years, but was designed to provide constituents maximum input into the decisions of the Board. Currently, a simple majority vote is needed to complete projects. The Board publishes all decisions via board minutes on its website and as a basis for conclusions within all significant standards.

The FASB develops major standards based on a conceptual framework. This conceptual framework was designed by previous Boards to act as fundamentals on which future financial accounting and reporting would be based. The conceptual framework, however, is not complete and is not consistent with all of existing U.S. GAAP. To address these issues, the FASB currently has a major project on its agenda jointly with the International Accounting Standards Board (IASB) to improve the conceptual framework and to readdress some major accounting standards where the application is not consistent with the conceptual framework or does not provide sufficiently transparent financial reporting. Areas being considered in this joint project include pensions, leasing, liabilities and equity, revenue recognition, and financial statement presentation.

Accounting standards resulting from the FASB process often leave open many questions of interpretation. The underlying reason for the need for interpretation generally results from either a misunderstanding of the stated principle or rule, or a concern that others will express a different view of the application of the principle or rule within the standard. The FASB staff offers a service to respond to inquiries, but exercises caution in answering some inquiries due to the establishment of precedent. Sometimes the FASB or FASB staff is asked to formally amplify or clarify a set of interpretive issues within an accounting standard. These interpretations were previously published as FASB staff question and answer documents with little Board oversight and no public comment period. Currently, these interpretations are primarily done through FSPs (FASB staff positions), which are discussed and debated with Board members at a public meeting and exposed for comment.

The subcommittee may wish to consider the process for setting standards and developing interpretations, including the FASB's voting procedures and the methods used by the FASB or the FASB staff to: (1) set their agenda, (2) set their priorities, (3) deliberate, (4) communicate, and (5) respond to technical inquiries.

Interpretive Guidance - EITF

In the mid 1980s, the FASB formed the EITF. The original charter of the EITF was to act as an advisory group to the Board to educate the Board on emerging issues so that the Board could decide whether interpretive guidance was necessary. Shortly after its creation, the EITF's charter was revised to allow for members of the EITF to develop authoritative interpretive guidance. The types of issues addressed by the EITF range from very specific to very broad, but are expected to be completed by the Task Force within one year. The EITF may only interpret existing standards and does not have the authority to amend or replace existing standards. Members of the EITF represent all significant constituents and include large and small preparers, large and small audit firms, and users. These members are volunteers and do not sever ties with their current employers or firms. The Chairman of the EITF is a member of the FASB staff and all documents produced for the EITF are developed by the FASB staff. A conclusion by the EITF is reached if not more than 3 members object. Currently, all conclusions by the EITF are exposed for public comment and are ratified by the FASB. This subcommittee may wish to consider the role of the EITF and whether that role should be changed to one of an advisory group.

Interpretive Guidance – SEC

The Commission itself sometimes addresses accounting issues directly. In addition, SEC staff primarily through the Office of the Chief Accountant (OCA) communicates to the public in various forms about accounting issues, including staff accounting bulletins, letters to industry, speeches, and other educational material. These sources of information often are viewed by the SEC staff as confirmations of existing accounting standards, but have led to restatements by public registrants. The OCA also receives requests from specific registrants for pre-review of accounting issues. These requests are often considered by others in determining their own accounting policies.

The SEC’s Division of Corporation Finance reviews and comments on financial reports filed by public issuers that are not investment companies. The Division has a process for making its comment letters public upon completion of the review process. Through the Division’s filing review process and its now more transparent process making comment letters publicly available on the SEC’s website, the staff of Corporation Finance can have a significant influence on how accounting standards are interpreted.

The SEC's Division of Enforcement, in the course of its investigatory and settlement negotiation processes, often explains the staff’s views of a registrant’s accounting conclusion. The Division’s communications in this regard have been viewed by some as representing views applicable to all companies and not just with respect to the individual facts and circumstances involving the party involved in the particular enforcement investigation.

This subcommittee may wish to consider the extent to which the SEC should publish interpretive guidance, as well as the communication methods used to describe the activities of the SEC or the SEC staff.

Interpretive Guidance – Other

Many organizations, including large accounting firms and the AICPA, publish detailed educational material regarding accounting. These publications are widely used and presumed to be correct by their readers, but may turn out to be not always consistent or accurate. When an inconsistency or inaccuracy is discovered, the authors of the education material often seek clarity from the FASB or SEC staffs. This subcommittee may wish to consider whether the FASB or SEC should be involved reviewing or providing this type of guidance.

The Use of Cost-Benefit Analysis in Standard Setting

Determining the costs and benefits of a new accounting standard or rule involves difficult predictions. Often, the true costs and benefits may not be able to be fully known or understood until after the new standard or rule is fully implemented. The processes and practices both pre- and post-issuance may differ among organizations that set accounting standards and rules. The subcommittee may wish to review the existing cost-benefit analysis practices of appropriate organizations to determine if changes should be recommended.

Existing Standards
This subcommittee also may wish to consider whether to review two or three previously issued standards or rules to understand both the cost-benefit analysis that was utilized prior to the standard or rule's exposure to public comment and the cost-benefit analysis that was utilized prior to adoption of the standard or rule. This subcommittee may wish to review whether any changes by the standard setter as a result of a given cost-benefit analysis or for ease of implementation actually reduced the costs of application or increased the benefits. Finally, the subcommittee may wish to consider two or three existing standards and determine whether any changes might be made to the standards to reduce the actual costs of application or improve the benefit to users.

III. Audit Process and Compliance
This subcommittee will study the current process of regulating compliance with the accounting and reporting standards and other environmental factors that drive unnecessary complexity, including the possibility of being second-guessed, the structuring of transactions to achieve an accounting result, and whether there is a hesitance on the part of professionals to exercise professional judgment in the absence of detailed rules. This subcommittee may wish to consider the following:

Financial Restatements
A significant number of restatements have occurred in the U.S. financial markets over the past few years. Some have attributed these restatements to more rigorous interpretations of accounting and reporting standards by preparers, outside auditors, the SEC, and the PCAOB, while others believe the concept of materiality (and discussions regarding materiality in SEC Staff Accounting Bulletins 99 and 108) is applied too broadly. Many believe that this increased volume of restatements makes it more difficult for securities analysts and other users of financial information to determine the significance of a restatement. Further, some have expressed concern that the high volume of restatements could lead to an environment where users of financial reports begin discounting the importance of restatements (for example, if restatements are viewed to be routine).

The U.S. Treasury has announced it is commissioning a study to determine why the volume of financial restatements has risen so sharply, and this subcommittee should monitor the U.S. Treasury's work in this regard. This subcommittee also may wish to consider the reasons for an increase in restatements. For example, the subcommittee might consider whether the increase is a result of: (1) a broad application of the definition of materiality (including the application of materiality guidance in situations where errors do not impact the "bottom line"); (2) more rigorous auditing or enforcement; (3) second guessing by the SEC, the PCAOB, or outside auditors; (4) increasingly detailed accounting standards; or (5) inappropriate application of standards by preparers/auditors. Further, the subcommittee may wish to consider whether there are alternative methods to communicate with the capital markets for certain types of accounting errors (including consideration of the potential for prospective methods to deal with making changes to historical accounting practices).

Use of Judgment

Any move toward reducing complexity and increasing transparency should consider the role of preparer and auditor judgment as it relates to the reduction of prescriptive application guidance. For example, one approach to consider could be whether to expand the use of accounting and auditing standards that allow for more judgment in application. The subcommittee should also consider the role of disclosure in such an environment. For example, some have suggested that more latitude should be provided in standards, with the caveat that more disclosure is provided about the alternative(s) that were considered and why the selected alternative was applied. This subcommittee may wish to consider whether an increase in the use of judgment (elimination of bright lines and detailed application guidance) would result in increased usefulness of financial reports, including the potential impact on comparability. Furthermore, the subcommittee may wish to consider whether an increase in judgment on the part of preparers and auditors is impacted by not knowing or understanding how these groups will be judged by the SEC, the PCAOB or others.

PCAOB

The PCAOB is required to inspect annually all registered public accounting firms that provide audit reports for more than 100 public companies, and at least triennially registered public accounting firms that provide audit reports for fewer than 100 issuers. Reports on these inspections have been produced in many cases more than one year after the completion of the inspections. Pursuant to the Sarbanes-Oxley Act, a portion of the results of the inspections are made available publicly, and certain nonpublic portions of the reports may remain nonpublic if the firm responds to the criticisms to the Board's satisfaction within a given time period.

Similar to the FASB, the PCAOB receives requests for guidance on how audits should be carried out. In the case of internal control reviews, the PCAOB issued a series of questions and answers, which were generally well received. Nevertheless, these questions and answers were issued without advance notice or public comment, despite the fact they were intended to have general applicability.

This subcommittee may wish to consider the PCAOB's inspection process and how the process impacts registrant and auditor behavior. The subcommittee may also want to consider whether this creates the need for additional auditing and accounting interpretive guidance, as well as the process on how such guidance is issued.

SEC – Corporation Finance

The SEC is required to review filings by listed public issuers on a regular and systemic basis, as well as review all public companies required to file reports at least once every three years. These reviews may be time consuming and are conducted by the SEC Division of Corporation Finance. A perception may exist that consultation with the OCA does not generally occur unless the registrant requests such consultation. This subcommittee may wish to understand the process the SEC uses to review registrants' public filings, including the process for providing comments and the level of review and coordination with the various departments of the SEC. Furthermore, the subcommittee may wish to consider whether and how the process impacts registrant and auditor behavior and creates the need for additional auditing and accounting interpretive guidance.

SEC – Division of Enforcement

The Division of Enforcement has broad authority to open an informal inquiry into a registrant's financial reporting or an auditor's application of professional standards with respect to registrant reporting. Formal investigations that provide subpoena authority are made only after approval by the Commission. The OCA is generally consulted before consideration by the Commission of a recommendation by the Division of Enforcement involving financial reporting or auditor misconduct. This subcommittee may wish to understand the process the SEC uses to open an enforcement investigation, including the level and timing of coordination with the various departments of the SEC. Furthermore, the subcommittee may wish to consider how the process impacts registrant and auditor behavior and affects the need for additional auditing and accounting interpretive guidance.

Audit Firms

This subcommittee may wish to consider whether the behavior of audit firms creates or results in unnecessary complexity. For example, to promote efficient and effective audits, audit firms have created various tools and controls so that a uniform policy is applied throughout their organizations. These include checklists, audit programs, training, and networks of subject matter experts. These subject matter experts tend to view their particular issue as very important and may insist on a uniform national policy, even if the recommended approach is not applied uniformly in practice by others outside the firm. This subcommittee may wish to consider the impact that these practices have on promoting judgment and transparent reporting in the capital markets.

Sustainability of the Audit Profession

Legal risks faced by audit firms and registrants clearly influence their behavior in preparing and auditing financial reports, including their willingness to exercise judgment and to show flexibility in applying accounting rules. With respect to audit firms, the U.S. Treasury has announced its intention to establish an advisory committee to study the sustainability of a strong and vibrant public company auditing profession. Treasury has announced that the committee is to study, among other things, the ability to attract and retain the human capital necessary to meet developments in the business and financial reporting environment; audit market competition and concentration; and the financial resources of the auditing profession, including the effect of existing limitations on auditing firms' structure. This subcommittee should be aware of how litigation and potential litigation influence behavior and may wish to consider the work of the Treasury's committee, but should not attempt to develop proposals that duplicate the work of that committee.

IV. Delivering Financial Information

This subcommittee will study the current system for delivering financial information to investors and accessing that information. This subcommittee may wish to consider the following:

Tiering of Information

Different groups of investors exist in our capital markets and may have different needs for information from financial reports. The individual investor may be interested mainly in a journalistic outline of the key points about the progress of the business. By contrast, a sophisticated investor may be interested in a full discussion of management's choice of assumptions underlying the financial reports as well as a comparative analysis of particular financial indicators versus a peer universe. Many have suggested tiering the information with a journalistic summary at the beginning and more detailed analyses as the reader continues to read. Within the context of the Internet, this could mean a summary page, together with hyperlinks to more detailed information on particular topics.

Tagging of Information

The SEC is engaged in a major project to introduce interactive data tagging technology for the informational content of financial reports, such as through the use of XBRL, so that users have the ability to quickly and easily focus on the important information they desire in these reports. Moreover, tagging of information may allow investors to customize their needs based on their desired level of detail. The tagging of information can be focused on performance metrics for carrying out the strategy of a specific company and could be designed along the lines of a balanced scorecard. The tagging of information can be organized into a variety of standard formats for key performance indicators (KPIs) organized by industry. An existing project for the development of these KPIs is being undertaken by a non-profit consortium on enhanced business reporting (originally started under the AICPA). The subcommittee may wish to study these developments and consider whether additional recommendations can be made to improve the usefulness of financial reporting in these areas.

Press Releases and Website Disclosure

Press releases and corporate websites have become important forms of communication for many public companies. For example, some companies post or issue press releases to report interim and annual results and in doing so often release non-GAAP financial measures. These operating results are often issued well before the formal operating results and disclosure are required to be filed with the SEC, and they may contain additional information that is not required to be filed. Recently as a result of implementing the Sarbanes-Oxley Act, the SEC revised its rules and regulations concerning the public disclosure of non-GAAP financial measures, including in press releases and earnings webcasts, and whether press releases also must be filed versus furnished with the SEC. This subcommittee may wish to consider the underlying reasons why press releases and web disclosures—and the information contained in them—are used by our capital markets in order to determine if additional performance indicators would be useful for our capital markets. In addition, the subcommittee may wish to consider the experience of issuers with disclosure of non-GAAP information and the use of press releases and corporate websites in connection with their financial reports. The continued demand for these disclosures by issuers may suggest that the required formats for reporting financial information are not serving all the needs of preparers and users.

Legal Issues

To provide various forms of communications that meet the needs of different investor groups, there may be a need to consider the legal liabilities for different types of information – e.g., MD&A versus audited income statements – and for the different communication methods used to provide them. For example, this subcommittee may wish to look at the experience with "free writing" in public offerings whereby issuers can communicate new developments or pieces of information that may not be included in the formal prospectus. Further, this subcommittee may wish to look at the various attempts to provide a summary prospectus in the mutual fund industry.

V. International Coordination

This subcommittee should consider whether the growing use of international accounting standards has an impact on the relevant issues relating to complexity of U.S. accounting standards and the usefulness of the U.S. financial reporting system (for example, by identifying best practice employed internationally). As it relates to the acceptance of International Financial Reporting Standards, or IFRS, in the U.S. capital markets, the SEC has issued a proposing release to permit the use of IFRS by foreign private issuers without a U.S. GAAP reconciliation. In addition, the SEC has voted to issue a concept release on whether U.S. issuers should be allowed the choice to use IFRS to satisfy their SEC reporting requirements. The SEC expects to receive important feedback on these initiatives that could be considered by this subcommittee. Each of the four other subcommittees should consider whether there are areas or international best practice that should be evaluated by the international subcommittee for implementation in the U.S. financial reporting system. Given the timing of the expected comment letter process on the Commission's initiatives, and in order of the other subcommittees to identify areas of focus, the substantive research and analysis of this subcommittee will not begin until early 2008. While the nature of the items considered by this committee has not been fully developed, the subcommittee may wish to consider the following:

Standard Setting Approach
This committee should consider whether there are "best practices" employed by the IASB in the standard setting process. For example, many believe the IASB takes an approach based more on principles rather than detailed rules, but the IASB, like the FASB, nevertheless does have conflicting principles and controversies based on volatility and the increased use of fair value. Many have observed that the accounting standards promulgated by the FASB are too lengthy. This is partly because the FASB includes in its standards not only the text, but also its history and the responses to significant comments on the initial proposal and implementation guidance. By contrast, IFRS generally include only the text in its accounting standards. The FASB has already started to work together with the IASB in formulating new accounting standards or revising existing standards in the hopes that future standards will be converged. The subcommittee may wish to consider a few examples where the FASB and the IASB are working together to determine if the process is effective and efficient to meet the needs of our capital markets.

Regulation
The enforcement of accounting standards outside the U.S. may be quite different depending on the particular jurisdiction from the enforcement policies and practices within the U.S. The subcommittee may wish to consider these differences and determine whether the U.S. system could benefit from any lessons from the foreign experience.

EXHIBIT C

Index of Written Statements Received

Listed below are the written statements received by the Advisory Committee before its first meeting on August 2, 2007 and the dates of receipt.

Aug. 1, 2007	Walter P. Schuetze
Aug. 1, 2007	Ralph D. Allen, Managing Partner, BeaconAdvisors, Financial Communication experts, South Salem, New York
Jul. 28, 2006	Gordon E. Goodman, Trading Control Officer, Occidental Petroleum