ASSOCIATION OF CORPORATE COUNSEL

Title: Hot SOX: Executive Compensation and other Sarbanes-Oxley Developments

March 14, 2006
12:00 p.m. CT

Operator: Just a reminder, today's conference is being recorded. The Webcast will begin in 10 seconds. If you have any technical questions or problems, please e-mail us at accwebcast@compartners.com. Thank you.

Please begin, (Jonathan Spencer).

(Jonathan Spencer): Thank you. First, I'd like to welcome everybody to – on behalf of the Small Law Department Committee of the Association of Corporate Counsel to our Webcast on Hot Socks Executive Compensation and Other Sarbanes-Oxley developments. Today we are going to cover some of the recent FCC proposals regarding changes to executive compensation as well as bring an update on developments under Sarbanes-Oxley, particularly as it relates to small companies and for small law departments.

A couple of mechanics before I do introduce all the parties, one, if you have questions, there is a box in your lower right-hand corner of your – of the Web page that you're looking at. Type your questions into the box and then press "send" and we will – we will take those in turn, particularly towards the end of the Q&A session.

Secondly, I'd like to remind people that at the end of the Webcast, there is a link, underlink that says "Webcast Evaluation", and we request everybody to complete that survey, and that would be appreciative.

So now I'm going to introduce our speakers who are all from the firm of (Hollander Knight). Our first speaker is going to be (Jayne Tam). (Jayne) devotes all of her practice to (reps) and corporate clients from promising (startups) and established domestic and international corporations. Ms. (Tam's) the principal outside counsel for domestic and foreign companies on securities offerings, FCC compliance, periodic filings, corporate governance, mezzanine investments, venture capital financings, mergers and acquisitions. This (Tam) is going to be speaking. In addition, we have also – and she's a partner at the firm of (Hollander Knight).

Also partner of the firm is (Jonathan Wolcott). (Jonathan Wolcott) practices in the area of securities, mergers and acquisitions and corporate law. He represents a wide variety of public and private companies, investment banks, private equity banks, and individual investors in structuring and executing public and private equity and debt offerings.

Our third speaker today is going to be (Mark Torallo). (Mark) is a member of the Business Law Department. He practices primarily on corporate and securities. He represents both public and private companies and startups, to publicly traded multi-national corporations. He represents both buyers and sellers in mergers and acquisitions and accounts and clients connections with public and private securities.

I'm going to again, we're thankful to (Hollander Knight) for doing this Webcast, and on behalf of the Small Law Department Committee, I'm now going to turn the program over to Jonathan Wolcott) who is going to start the presentation.

(Jonathan Wolcott): Thank you, (Jonathan), and on behalf of (Hollander Knight), we want to thank the Association of Corporate Counsel for this opportunity to speak today. We thought today, rather than rehashing the nuts and bolts, Sarbanes-Oxley information, that we laid out in our (SOX primer) came out in September, we would address some recent developments and securities law that we thought would be of interest to you all.

First, I'm going to discuss the executive compensation proposal. While this proposal is not technically ((inaudible)) under Sarbanes-Oxley, it's a logical extension of the kinds of rule-making we've seen under (SOX), mainly more and fuller disclosure of the policies and procedures at the top levels of public companies. In response to some of the corporate mishaps that led to (SOX), the proposed rules would shine a brighter light on how executives are (incentivized) and how directors reach decisions to provide those incentives.

The rules were proposed in late January and comments are due on April 10th. While it's not a certainty, it's presently likely that the rules would be in place for the 2007 proxy season. The proposal is a comprehensive and detailed overhaul of the executive comp disclosure rules that covers, I think, 370 pages of ((inaudible)) per issuance. I'm ((inaudible)) I'm just going to hit a few of the highlights here and I'm going to provide a couple of recommendations of some action items for you and your companies to consider.

The first major change in the Executive Compensation Rules is the requirement to include a compensation discussion and analysis. And more or less what this is, is (MD&A), Management Discussion and Analysis, as applied to executive compensation. Basically, what the FCC is looking for here is the why and how of executive compensation, the philosophy the company has about executive compensation and how they enact that philosophy.

This – the propose – they're calling it (CD&A) now, would replace the Compensation Committee Report and the stock performance graph that's currently included in Executive Compensation

sections. And it would require companies to address the objectives and the implementation of Executive Compensation programs.

Among the requirements the FCC has proposed that the addressed are all the elements of the executive compensation, the specific items of corporate performance that usually the compensation committee takes into account in setting comp policies and making compensation decisions, and how each of those elements of compensation fit into the company's overall objectives.

It would also require the company to address any material differences among the named executive officers, notice the top five that are required to be – whose conversations require to be disclosed in detail. For example, if you're a CFO and your CEO has an incredibly different compensation scheme and numbers, the (CD&A) should address why that is.

And finally, the (CD&A) would be considered (styled) with the FCC as opposed furnished. Currently the Compensation Committee Report is furnished with the FCC. And what this leads to is that it would be covered under the CEO/CFO certifications under Sarbanes-Oxley Section 302 when the Executive Comp sections are incorporated by reference into another filing. For example – perfect example is your 10K.

So now instead of your Compensation Committee just signing their report, the sort of broad discussion of compensation policies would really fall under management's view. Management would be responsible for the accuracy of it. In addition, the (CD&A) would be subject to Section11 under the Securities Act Liability when it's incorporated by reference into a registration statement.

The next sort of big overhaul is the summary compensation table, and what we've provided here is what the FCC has proposed it looks like. And I'll just walk you through a couple of – couple of

changes here. The first major change you'll see is in column C, which is the total compensation number. Currently, this doesn't exist. And what this really is, is a total – sum total of the other columns that are in there, salary bonus, stock awards, option awards, incentive plan compensation and the broad catch all of all other compensation. And again, we have a top five here as we currently do under the rules, but one major difference is that the principles – what they're calling the principle financial officer, usually your CFO, would be automatically included as the top five member regardless of compensation level.

As I said, (here) are the noteworthy changes, our total annual comp and that the principle financial officer is now included. And calculating the values of stock based awards, companies would be required to calculate them in accordance with new accounting policy 123R, which basically values stock base awards at a grant date value and using some sort of (black shows) model or other formulating consumptions.

And the FCC, in the new proposal, would require companies to reference to those assumptions, in other words, how they arrive at those values. There's a lot of different elements, as some of you may know, that go into those. My guess is that probably you're not just going to make reference to (MD&A). What you're going to see people do is actually include a full fledge discussion of those assumptions in your – in your executive comp section. And in addition to the – to the table, narrative disclosure is required with regard to mature elements of compensation that sort of don't come through with just – on a pure numbers basis.

This is sort of the same throughout the new rules, is that instead of just placing tables up there and planting numbers in them, the FCC wants companies to discuss things and to provide sort of fuller material disclosure where necessary to shine the line up on the numbers. And the FCC wants all of the new Executive Comp section to be in plain English.

One other major change is that the determination of your top five, your main executive officers, will be determined on the basis of the total compensation number as we showed you on the table before. So it's the sum of all compensation. Currently, as you may know, it's just salary plus bonuses that determine the top five.

So, as a result, it may change for a number of companies who your main executive officers are and as a result, who gets disclosure on their compensation.

The FCC feels that the current director compensation, which is for almost every company just provided it in a narrative form is an aware (under) whelming, and they want fuller disclosure of director compensation and poor disclosure of all elements of director compensation. So what they – what they required in the new rules is tabular table very similar to the summary compensation table that we showed you earlier, and also narrative disclosure with regard to directors.

One interesting element of this is that in the summary compensation table, prerequisites would have to be disclosed for executive officers on a much broader basis than they currently are, and this would also extend to directors. Currently I think, you know, a lot of companies just sort of, you know, provide a boiler plate statement that we reimburse, you know, for these costs. But if directors are actually getting perks, it would now have to be disclosed both on a numerical basis and on a narrative basis.

The FCC, in the new proposal, has put forth revisions to Form 8K with regard to current report disclosure of material compensation arrangements. What they say in the proposal is that they feel that companies are providing a lot of non-material disclosure in this regard, and this is under item – currently under item 101 of Form 8K. And they don't really tell us what they think is being (over-disclosed) in this regard, but this is the kind of disclosure you see companies doing, for example, when compensation is set for the year for the executive officers. Sometimes you'll see

companies do tables that set up with the comp committee has set for new compensation targets, and salary, et cetera under item 101.

More or less what the commission has done in this regard is just move a lot of those requirements to item 502 of Form 8K. And what item 502 currently does is requires disclosure of certain triggering events like resignations and employments of executive officers and directors. And so they've moved a lot of the disclosure in there, but from what we can really tell and I, you know, if anybody wants to chime in on this, be my guest, but I don't think really disclosure in this regard is going to change all that much.

I think what you're going to see is people continue on the same path, just under a new item number. The consequences of not disclosing material compensation arrangements on a timely basis are somewhat severe, although under the new proposal, as under current rules, you wouldn't be penalized and lose S3 eligibility if you were late in filing an 8K with regard to material compensation arrangement.

But, I guess what you really have is a (pass) until your next 10Q or next 10K. So if you didn't file within the four days, you'd be OK. But if you didn't get it in by your next 10-K or 10-Q that's due, you would lose your S3 eligibility, and they've kept that under the new rule.

Male: (Jonathan)?

(Jonathan Wolcott): Yes.

Male: Just to comment on the 8K, I think the main change is that a lot of (accounts) have been advising to file 8K's for any sort of change in compensation since they would be material. So I think that this will eliminate a lot of those tables.

(Jonathan Wolcott): Yes, it might – it might. But, you know, I think because of the consequences of it, if you ever ultimately fail to file, I think what we need to see is some guidance from the FCC to say, what do you think we really are over-disclosing? You know, if it comes down to a judgment call – yes, sometimes you can see very easily, this is material, this is not – not every option award needs to be disclosed, and they've made that clear through their FAQ's and things like that. But, you know, it is – it does, (Jonathan), it turned out to be a judgment call and I think some people are going to, you know, still continue to (error) on the side of caution.

So what I'd like to see from the FCC is something in the final rule that says, this is what we think, you know, more or less, or give some examples of things of what they think is over disclosure.

Any of USB filers out there are going to get some significant release, excuse me, from the proposed rules. Small business filers are not going to be required to provide a (CDMA). They're only going to be able – only going to have to provide information in the summary compensation table for the last two years as opposed to the last three years for other filers, and only three executive officers would be covered. It would be the principle executive officer and the next two most highly compensated officers; small business filers; CFOs would not necessarily be included in the summary compensation table and be named Executive Officer.

The FCC also proposed some broad based changes to disclosure of related party transactions, and what they've gone through here is instead of sort of the hodge podge of criteria under current (Reg FK) Item 404, they just – they've (propagated) a principles-based approach. And what they've said is they've – they don't want to sort of define related party – they provide us sort of a definition of related party transactions that instead of having some bright light rules, focuses a little bit more on materiality. And the elements of related party transaction of the proposal are any completed transactions since your last fiscal year, or any currently proposed transaction in which the company is or was a participant where the amount involves 120,000 or more, and a related party has a direct or indirect material interest. And the definition of related party, which currently

covers directors and executive officers and I think immediate family members would be broadened a little bit to include step children, step parents, and people who live in the executives house other than employees and tenants.

So the focus here is more or less on the material to investors. And in the proposal the FCC sites material ((inaudible)) standards under cases like (Basic V. Levinson), to guide companies into, you know, what is material to investors in this regard.

In addition, there's a statement in the proposal that says that, you know, don't count on the $120,000 limit as a threshold as a bright line rule. You really got to look at every single related party transaction and determine its materiality. The 120,000 is the rule, but if something is truly material to investors, you probably want to disclose it.

One of the most sort of timely things the FCC did in the – in the proposal is to provide some really currently applicable guidance as to what a prerequisite is. And a lot of people have focused on this immediately because they felt it was applicable to their current processes. What the FCC said with regard to prerequisite, it's some sort of an item to an executive officer or director that confers a direct or indirect benefit that has a personal aspect to that – to that person, regardless of whether or not it may be provided for some business reason.

What they're getting at there is something that has a quasi business reason, but also has a personal aspect. If that's the case, it's a perk unless – and there's a couple of exceptions here – unless it's not a – unless it's available on a non-discriminatory basis to all employees. And the other exception that they have – that they have put forth is that if the item is in to really and directly related to job performance, then it's not a perk. But they have cautioned all of us that that – the (in to) really and directly related to job performance, then it's not a perk. But they have cautioned all of us that that – the (inter-really) and directly related to job performance exception should be construed extremely narrowly.

And lastly, disclosure for prerequisites is not required until the aggregate of all perks gets to $10,000. But after that point, any perk that – any and all perks must be at least separately identified. And then if a perk – an individual perk exceeds the greater of $25,000 or 10 percent of all aggregate perks, you've got to actually quantify it as well as disclose it sort of in a narrative format.

So, more or less, we're lowering the threshold significantly here as to perks, and I think you're going to see companies maybe treat perks differently in terms of how they're (delve) out and certainly track them a lot differently than they currently do.

We've included here some of the examples the FCC has set forth in the proposal with regard to what's a perk and what's not. I welcome you to all – I'm not going to go through this – but I welcome you all to look at this at your leisure after this Webcast, and these sort of provides some guidance for you.

We have a couple of humble recommendations to you all with regard to things we think, you know, you should start thinking about or even doing in light of the proposals. Now, proposals may change but certainly per former rule proposals, a lot of the stuff that we saw the (rule proposal) will remain in tact.

I think it's a good idea at this point to at least inform your compensation committee and your CEO and CFO, at least a summary of what this is – get them, you know, get them thinking about what's going on, you know, how this is all going to change. And, you know, you need to let them know that because of the timeline for enactment of these rules, that compensation decisions that are being made this year are probably going to have to be disclosed next spring if you're a calendar year company, that is, in your proxy statement and 10-K's, incorporated by reference.

So, you know, even decisions that were made in January on compensation, when everybody didn't know the full extent of these rules, although we kind of all knew it was coming, they're going to have to be – they're going to have to be disclosed next year more likely than not.

One thing that, you know, you might want to do, as in-house counsel to the extent you have time and the inclination is, when you – when you read through the rules or read through a summary of the rules, you know, sort of perform your own kind of individual audit and think about, oh – OK. This is going to change, this is what's going to change for us and maybe keep track of those things yourself and use that as a basis to inform your CEO and your compensation committee. And you need to let your CEO and CFO know that no longer is the sort of broad based discussion of compensation philosophy or practices that's currently on the comp committee report, no longer is that just the responsibility of the compensation committee. That is going to be something that they're certifying to in their 302 certifications.

In terms of determining who your top five are, you know, you got to let your CFO know. If he's not currently a top five member, he's going to be next year or when the rules are probably – ultimately passed. And then, you know, as I said earlier, the three other executive officers that are going to be in the top five, are going to be determined on the basis of total compensation, and that may change who your top five are.

In terms of perks, as I mentioned, companies may want to, from an accounting perspective, you know, if you have sort of internal mechanisms to keep track of perk disclosure, you're going to maybe want to change those around and, you know, you may want to do that through your – through your accounting people based on the new rules proposals. You know, the threshold's now 10,000 in the aggregate, and that may change the way you look at – you look at the way you keep track of things that are provided to your executive officers, and remember, to your directors as well.

In terms of related party transactions, one of the rule proposals would require not only disclosure related party transactions, but a disclosure of the policies and procedures the company goes through to approve related party transactions. And so, you want to maybe take a look at the way that those are done in your company, so in other words – so that you can make the disclosure so that, you know, you know what the disclosure will look like.

One other proposal that the FCC made, which is a completely new disclosure item, is that any shares pledged by an executive officer, a director or a nominee, would be required to be disclose, I think – I think it's probably as a footnote, to the beneficial holders table. So, you might want to look at your policies for approval of pledge shares. A lot of people have them and they're inside our trader policies, and if you do, that's great. But you also want to maybe enlighten your executive officers and your directors know that if they go out and pledge shares, the world is going to know about it.

And then another change in the rules may require some sort of an immediate action on your part is, is with regard to post-employment payments. Currently, a lot of people simply in a narrative format, disclose what the change of control or retirements benefits are and their employment agreement. This all now will have to be quantified, including an estimate of benefits and the like. Things like health insurance that's not sort of readily, you know, available. There's no set number. But that means you're going to have to estimate what these are.

And so you're going to want to take a look at your post-employment benefits that you provide your executive officers and, you know, tally them up and see what it comes up to, and start thinking about how you're going to estimate health benefits and things like that so that, you know, because that number could get very large. And certainly, that could provide some interesting information to the world if that number's, you know, very significant.

With that, I am going to turn over to my colleague, (Jayne Tam), who is going to address some of the recommendations and the status of the FCC's advisory committee on small companies.

(Jayne Tam): Thank you, (Jonathan).

Let me get the …

Male: (Jayne), you're going to have to come close to the phone.

(Jayne Tam): Oh – what about now. Is it better? Is it better now?

Male: A little bit better, but I think you need to be a little closer.

(Jayne Tam): OK – what about now?

Male: I think that's good.

(Jayne Tam): OK because I can't get any better than this. OK – let me make sure I have control of the slide here. OK. For the next 15 to 20 minutes or so, I would like to talk to you all about an exposure draft of the final report published by the Advisory Committee on Smaller Public Companies just about two weeks ago on February 27th.

The Advisory Committee on Smaller Public Companies was chartered by the FCC about a year ago, on March 23, 2005. The objective of the committee was to assess the current regulatory system for smaller companies under the securities laws and recommend changes. Members of the committee include representatives from smaller public companies, William Blair & Company, Deloitte & Touche, Venture Capital Services, (ABMG) and many other distinguished trade associations and industry leaders.

On or before April 3rd, you may send your comments on the draft report to this Web site that I have on this slide right here, or send an e-mail message to (rule-comment@fcc.gov), and include on the subject line, the fie number. The final report is scheduled to be released at the end of April of this year.

Now one thing to note is this is – the Advisory Committee on the Smaller Public Companies are totally separate and apart from the FCC. So this is not to be confused with the rule proposal such as the one that Jonathan just talked about on ((inaudible)) comp issue. This is merely a committee that was chartered by the FCC to do certain studies about the impact of the current regulatory system on smaller companies. So to the extent and the even that the FCC will consider or adopt any or all of the recommendations by this advisory committee, you know, we won't see that probably until later part of the year at the earliest.

I need to make sure I go to the next one.

The areas of review, let's talk about the scope of the review here. The committee has focused their review on four specific areas, including the impact of Sarbanes-Oxley Act of 2002 in each of these four areas: internal control over financial reporting; the very infamous or famous Section 404; conference disclosure and reporting requirements and federally imposed corporate governance requirements; accounting spend and financial reporting requirements; process requirements exemptions related to security offerings. Over the past 10 to 11 months, the committee actually conducted interviews and studies, prepared testimony and reviewed comment letters in these four areas.

What are the objectives of the advisory committee? They are to conduct a cost benefit analysis to assess whether the cost imposed by the current regulatory system on smaller public companies are proportionate to the benefit; to identify methods to minimize cost, facilitate capital

formation for smaller companies and to recommend a regulatory regime that allows scaled or proportional regulatory treatment for companies based on their size without compromising on good corporate governance and transparency.

One of the first things that the committee did was that they set up a “size taskforce”. They need to define what should be considered smaller public companies. The committees very quickly have adopted or have come to using the market (tab) as a way to measure a size of a company. The lowest one percent of the total U.S. equity market capitalization would be considered – companies representing the lowest one percent would be considered “micro cap” companies. And companies representing the next lowest five percent of U.S. equity market cap would be considered small cap companies, and I’ve also laid out on here, you know, what that would translate into in terms of the number of millions of dollars in market (tab). And smaller public companies would be defined to include these two categories.

So in other words, smaller public companies with a purpose of this review by the advisory committee would focus only the lowest six percent of the U.S. equity and market capitalization. However, it’s very noteworthy that these – the lowest six percent actually represent close to 80 percent of all of the U.S. public companies.

And you will quickly notice that the advisory committee has decided to use (market tab) instead of public float as a way to measure size. You know, the FCC has always been using public float as one of its measure of stratifying – of categorizing different categories of public issuers. And in the – in the draft report, the advisory committee has cited many advantages of using market (tabs) instead of the public float as a yardstick. And one of the reasons cited was a particular way to subjectivity invariably gets into the way of determining which holdings would count to a public float and which wouldn’t. But quite honestly, I think that would be – that would really require some ((inaudible)), you know, from the FCC – to the FCC to sway them, you know, to this other direction which is different from what the FCC has been doing in recent years.

But then considering that, you know, (John White), the new director of the Division of Corporation Finance, will be starting exactly in four days ((inaudible)) when it happens. But I just thought that it was interesting that they – that this advisory committee has actually decided to look at market cap instead of public float.

The committee has actually came up – come up with 32 final recommendations to ease the regulatory regime that currently applies to smaller public companies. Obviously, I don't have time this afternoon to talk about all 32 of them, but I have picked out what I would consider to be the top five recommendations or at beat other recommendations that have generated the most debate over.

When you read the report, you'll see that the committee has come back again and again to the fact that since we are only talking about changing the rules that apply to the lowest six percent of the U.S. equity and market cap companies, even if all the 32 recommendations are adopted, the full benefits and protection of the federal securities regulation for companies as well as investors, in 94 percent of the total public U.S. equity capital markets will remain intact. So …

Male: (Jayne).

(Jayne Tam): Some people are still having trouble hearing you, so if you could speak louder. The other thing is, unfortunately, (Jonathan Wolcott) went a little long, so I'm just going to ask you to move a little faster through – to the recommendations.

(Jayne Tam): Yes, I will – I will certainly do that. I will try to shout as much as I can.

So, to the extent that the regulations have this (proportionate) impact on the smaller companies or that the public interests are outweighed by the (cause), the committee is advocating that we should scale the regulation for certain public companies based on size.

The first recommendation I would – I would – I would want to talk with you all is about scaled financial statement accommodations under Regulation (SB), to be made available to all smaller public companies. As we all know, the FCC adopted Regulation (SB) in '92 allowing companies with revenue and public float of less than $25 million to use a set of abbreviated disclosure rules scaled for smaller companies. In 2002, the FCC divided companies into accelerated and non-accelerated filers. In '04, the FCC added this third category of large accelerated filers, again using public float as the way to categorize the different – the different groups of public companies.

One of the things that the advisory committee is strongly advocating is to allow smaller public companies to also have the benefit of using these abbreviated disclosure rules on financial statements as well as actually disclosure accommodations as well, which we will, you know, talk about in a second.

Basically, just to put it, you know, just to summarize it, is to require smaller public companies to provide only two years of income statements instead of three, one year of balance sheet instead of two in smaller public companies annual reports and registration statements. The obvious benefit is that it would reduce cost, simplify disclosure, and lots of people argue the fact that in this dynamic economy, ((inaudible)) and corresponding analysis is generally less relevant. And when you have shorter periods of financial statements required to be reported, it generally means that it's easier for smaller public companies to change auditors should they see the need to.

I'm having difficulty ((inaudible)). The second recommendation that I would talk to you about is about exemption from Section 404. It clearly is by far the most controversial of the 32 recommendations that the advisory committee has put forward. Very briefly, Section 404 requires

all reporting companies to include in their annual reports a statement of management's responsibility for establishing and maintaining adequate internal control over financial reporting together with assessment of the effectiveness of those controlled.

Section 404 also requires that company's independent auditors attest to management's assessments. The smaller you are, the larger the hit. The expected cost of 404 compliance as a percentage of revenue is dramatically higher for smaller public companies than it is for larger public companies. And the – and the advisory committee has actually (studied) the fact that the London Stock Exchange (in markets), the alternatives investment market has reasonably – in recent years gained momentum. The fact that there are more companies that are going (dark), meaning that the reporting companies are filing Form (15's) to exit from the (34 Act) reporting obligations when they drop the (loads) of the 300 shareholder threshold, and that companies are going private in order to avoid the cost and burden of (SOX). And the advisory committee wants to use all those (historical) evidence to support the argument that the cost for especially for 404 among other, you know, (SOX) related compliance cost totally outweighed the benefit.

So one of the things that they talk about is for micro cap companies with these thresholds that I've cited in the slide, should be exempted from Section 404 as long as they would agree to the following three conditions: adhere to audit committee standards under Rule 10A3. Now as we all know, regardless, I'm sorry, regardless of whether they are listed on a stock exchange that has incorporated the (10A3) rules or not. As we all know, (10A3) is an expressed area of pretty comprehensive rules adopted by the FCC not too long ago that relates to the audit committee members, independents, responsibility of the audit committee about the procedures to receive and process accounting related complaints, the authority to engage their own advisor and all that. And the advisory committee is recommending that as long as companies would do that regardless of whether they are currently under the current rules required to do so or not, that should be a good indication of the internal controls in terms of the integrity of the internal controls.

((inaudible)) condition to this exempted relief would be to adopt and enforce a code ethics applicable to all directors, officers and employees. Under the current rules, issuers that are not subject to stock exchange listing standards requiring for such code of ethics are not required to do so. They don't have to adopt the code of ethics. The committee argues that the adoption and enforcement of such a code is both cost effective and appropriate for smaller public companies that we see such relief from Section 404.

And lastly, is the design and the ability to maintain effective internal controls over financial reporting.

On (extensive) relief from external audit involvement, that would be – to be exempt from auditor's ((inaudible)). Due to the lack of clear guidance on how to develop and support a proper Section 404 assessment of the effectiveness of internal controls, the advisory committee advocates that smaller public companies should be given exemption relief from this auditor ((inaudible)) portion of Section 404. Again, they agreed – I mean, they understand that they're also advantages to requiring certain other SOX requirements applicable to the smaller public companies and therefore, they have agreed in this study that it's important for certain conditions to be imposed on the public companies before this (exemptive) should be granted.

And these conditions would include your management's report on its assessment of internal controls, your Section 302 and 906 CEO and CFO certifications and again, you know, the ability to maintain internal controls designed to provide reasonable assurances to accuracy of financial statements.

In addition, the committee has also advocated that the FCC should allocate a Web site entitled something like, "Center of Excellence" for reporting and corporate governance for smaller public companies containing best practices, frequently asked questions, and complex transaction accounting advice. I think the committee has heard a lot of testimonies as well as, you know, a

lot of comment letters from the industry really, you know, requesting for more guidance on that front. So, you know, it would be a good thing if indeed the FCC would consider doing that.

And the last two recommendations I'm going to run through pretty fast is on the scale – disclosure accommodations under (SB) to be made available to small public companies again is back to the same thing of recommendations that I talked about earlier on the financial disclosure. They would want to have (scale) disclosure accommodation as well just to make sure that the smaller public companies, not so much govern by the public (float) under (SB) but also be able to have the benefits of the abbreviated disclosure rules.

And then briefly on the last recommendation I want to talk about is the fact that all exchange – not so much the fact, but the recommendation that all exchange or over the counter (bulletin board) listed companies that are current in their FCC reporting should be able to use Form S3. As we all know, the S3 allows the maximum use of incorporation by reference to information previously filed with the FCC. Since 1999, the OCC DB company has been required to file (34X) reports. Since then – and they also have the obligation to file current reports on Form 8K.

So the advisory committee's position is that as long as these public companies have been reporting for at least one year, so there are, you know, there's enough, you know, information in public on the ((inaudible)) and 8K and that they are current in their reporting at the time of the filing, the disclosure should be enough to protect investors and inform the marketplace about the development of these companies. And smaller public companies should be permitted to take advantage of the efficiency and cost savings of incorporation by reference to information already on file.

Of course, that would mean that, you know, if the FCC were to consider this, obviously that means, you know, a rule proposal to eliminate the current $75 million public (float) requirement

for primary offering for (S3) also if you eliminate the requirement for timing filing over the past 12 months.

And so, you know, that would be – that would be quite a change from the current, you know, (SB) regime as well.

With that, let me turn it over to my colleague, (Mark Torallo) who will talk to you about some other latest development on (SOX).

Male: (Mark), I just want to interrupt because we're running out of time here, you're going to have to be very brief so we leave some time for some questions.

(Mark Torallo): Sure.

Male: Go ahead.

(Mark Torallo): OK – thank you everybody for joining us today. I wanted to talk to you briefly about a couple of updates to some of the written materials that – things that have arisen since the white paper was published.

The first update or the first piece that I think is important is an FCC case dealing with loans under Section 402 of Sarbanes-Oxley. And Section 402 of Sarbanes-Oxley is one of the – one of the more clear cut sections of the statute. It basically says it's unlawful for any issuer to extend or maintain credit in the form of a personal loan for any officer or director. And at the time the white paper was written in '05, the FCC had not considered any cases dealing with violations of 402. But on December 1st of last year, of 2005, they issued an order in a case called ("Stellmar Shipping").

(Stellmar) was a foreign issuer that was listed, excuse me, on the New York Stock Exchange, and (Stellmar) had a CEO and CFO who approved loans for each other. And they tried to characterize these loan as advances of salary that would eventually get paid back, but they didn't document them in any way, they did not speak with outside counsel or the outside auditors in any way, and probably most importantly, they didn't speak with the board at all about these.

And the FCC basically shot down their argument that these loans should be treated as advances and instead took the view that these are what they are, they're impermissible loans under 402 and issued a (seize and resist) orders against both the CEO and the CFO with respect to any future violations of 402 of Sarbanes-Oxley, which is actually ((inaudible)) Section 13K of the – of the Exchange Act – of the loan prohibition.

So this may signal something more of a willingness on the part of the FCC to prosecute cases involving allegedly loans and it's just very important to bear in mind any time you get into a circumstance that could look like a loan, that it be considered very carefully, it be considered by the board, outside counsel and the auditors, and that every act – every care be taken to make sure that it doesn't want to follow a 402, because it is clear that, you know, there are things out there that will get the FCC's attention that will lead them to bring some of these enforcement actions.

Another area that has changed a little bit since we put the white paper together is the Section 404 requirements. (Jayne) touched on that a little earlier, and in fact, based on the advisory committee's report, or at least a portion of the advisory committee's report, last September, the FCC again extended the 404 compliance requirements for smaller companies for what they call "non-accelerated filers" to the first fiscal year that ends on or after July 15, 2007. It had been set at July 15, 2006. The way the rule is written, it means that, you know, any company whose fiscal year ends December 31, 2007 is going to have to be in compliance for all of 2007.

But this is the second time that the FCC has extended the 404 compliance period for non-accelerated filers, and again, given the small company's report, the advisory report, it is possible that they will look to grant some relief from the filing requirements for the smaller companies.

And I think with that, (Jonathan), if you want to stop there, we could probably jump into the questions.

(Jonathan Spencer): Yes.

(Mark Torallo): I think – I think we could probably end there and go into the questions if you would like.

(Jonathan Spencer): OK. Again, I'd like to remind people that they can ask questions by – in the lower right-hand column, there's a box marked "questions". If you type your question in there and then hit "send", we will be able to get your questions. And again, I'd like to also remind everybody that there's also a link under the "links" button for the Webcast evaluation so that when we're done, we'd like everybody to complete the evaluation/survey and get your responses.

OK. The first question that we have was done with the proposed compensation rule is, "When are those rules expected to go into effect? Obviously we noted the proposed rules, but can we ((inaudible)) when we think these will go into effect?"

(Jonathan Wolcott): This is (Jonathan Wolcott), you know, it's unknown; the comments are due on April 10th, and given, you know, the FCC's sort of normal (hedge) on rule makings of this size, if all goes according to plan, I think you might see something in late summer or early fall with regard to this – possibly at the earliest. Now, you know, if they're asked to go back to drawing board on some of this stuff, it might be a little longer. But, you know, under the proposed rule, as I mentioned, they'd likely be in effect for the – for the 2007 processes. And under the transition

proposal, proxy statements that are filed later than 90 days after the rule is finally published, will be subject to the new ((inaudible)).

So the most common ((inaudible)) possibly even (December 30th) ((inaudible)) depending on when they get the rule finally published ((inaudible)) annual ((inaudible)) proxy statements, you know, would be required to include this disclosure.

(Jonathan Spencer): OK. (Mark), a great question about the restriction on loans to top executive officers, and the ((inaudible)) on auto loans? Are there any exceptions?

(Mark Torallo): Well, the loan prohibition applies to loans for personal use. If there are loans for legitimate business purposes, such as, you know, company use of a credit card for company expenses, travel advantages, relocation expenses that are ultimately reimbursed but have to be of a business nature, those types of loan are still permissible as long as they are primarily for a business nature. It's really the personal nature of the – of the loan that causes a violation of 402.

For example, where you've got a credit card that has a mixed business and personal use, and it doesn't require immediate repayment of the personal aspect of it, that's a problem.

(Jonathan Spencer): OK. And so, for example, there's a question here, so a (bridge) loan (executive), that would be something ((inaudible)) would be prohibited?

(Mark Torallo): I would think so. There are some commentators who feel that relocation expenses, and I don't know if that (bridge) loan would be in a context of a relocation expense, they are permissible as long as they are repaid and there's a – there's a legitimate, you know, business purpose for the relocation expense. I mean, if you're – if you're relocating somebody to the headquarters in New York, that's a business purpose. If you're relocating them to West Palm Beach so that they can telecommute, I don't think that's probably going to be a problem.

(Jonathan Spencer): OK. Looking here to see if we've got any further questions. (Jonathan), I think we had a question on ((inaudible)) did the FCC give other examples of ((inaudible)) (perks)?

(Jonathan Wolcott): There are ((inaudible)) a section of the rules proposal with regard to prerequisites, and also on our slides, we've provided some examples of, you know, sort of (closer) issues on prerequisites here and I'm (flipping) through it right now. It's page 12 of the slides.

You know, one prime example of questions have come up are, you know, if you've got a – if you've got an (extra) secretary, normal the question is, is that, you know, is that a prerequisite to an executive officer? And really what it comes down to is what is that secretary being used for? Is it being used for directly and entirely for business purposes? Then it's not a prerequisite. But if its being used – the secretary's being used for partial personal business, scheduling vacations and, you know, making sure kids get picked up from private school, then that's a prerequisite. And then, you know, the (annual) cost to the company of that secretary's personal time or your time on personal matters is a perk. That needs to be disclosed.

I'd point to the section on prerequisites in the FCC proposal and to page 12 of our – of our PowerPoint here.

(Jonathan), I think somebody asked a question about – I think it was a very good question about who should divide – I think what the meaning is between management and the compensation committee, who should be providing the narrative disclosure in order – in order to provide the appropriate checks and balances on the disclosure. And that's actually a very interesting question. It brings up an issue with regard to the rules, especially the compensation discussion and analysis, the (CD&A).

Whereas this is supposed to be sort of company's philosophy on and policies on compensation which, you know, it's ((inaudible)) come from – should come from the compensation committee. That's what they're charged to do. And yet, you know, all of a sudden because this whole section is now deemed to be (filed), it becomes a province of management to determine whether these things are accurate. So it's a little bit of a strange ((inaudible)) there. But my suggestion, at least emotionally until we see some sort of ((inaudible)) some changes from the commission on this rule is that really, you know, I think management should probably take the first shot at it. I know the (CD&A) may come from compensation committee, but in the end, both parties have to review it very carefully. And the compensation committee certainly should review this in full in detail before it gets filed.

(Jonathan Spencer): OK. Thank you. I think we're just out of time here, so I'm going to wrap it up. Appreciate – again, on behalf of the Small Law Department Committee of the Associated Corporate Counsel, I want to thank (Jayne, Jonathan and Mark) for their presentations. I want to remind people to complete the survey by clicking on the link, the first link under the link box. And really, that's about it. Thank you everyone.

Female: Thank you.

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