August 31, 2005

Via Fax

Mr. Jonathan G. Katz, Committee Management Officer
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

Re: Request for Public Input by Advisory Committee on Smaller Public Companies (File Number 265-23) – 93

Dear Mr. Katz:

I appreciate the opportunity to respond to the request of the SEC Advisory Committee on Smaller Public Companies seeking input on issues related to the current securities regulatory system for smaller companies, including the impact of the Sarbanes-Oxley Act of 2002 ("SOX") on the system.

I believe that a balance must be struck, based on a cost-benefit analysis, of keeping our smaller public companies viable and competitive in business and the marketplace, while adequately protecting the integrity of the financial markets and the needs of investors for accountability by management. The first three years under SOX have clearly demonstrated the disproportionate burden of the cost of being public to smaller public companies, both in terms of financial resources and human capital. As such, a revisit of the cost-benefit analysis is a welcome development and the Advisory Committee should be thanked for its hard work in this endeavor.

My comments to certain of the Committee's questions follow, keyed to the specific number of the questions contained in Release No. 33-8599; 34-52189.

1. I have had numerous discussions with clients and prospective clients about the cost – in terms of both dollars and human resources – of going public and remaining public. Numerous already-public small companies have expressed concern about the disproportionately high cost of remaining public – they suffer a much higher percentage of their revenues in compliance costs compared to any other group of public companies in the US -- and frequently inquire about alternatives, such as filing a Form 15 or the procedures – and costs – of going private. However, many of these smaller public companies are not eligible to file a Form 15 and also cannot afford the high cost of going private in compliance with the "going private" rules (which have not been reviewed since the adoption of SOX) and the cost of carrying the buy-out debt. I would urge some

version of "going private light" be considered to grant relief to smaller public companies who can no longer afford to remain public and cannot afford to "leave the playing field" by going private under the current system.

2. Generally speaking, I do not believe that SOX has affected the relationship of smaller public companies with their shareholders.
3. no response
4. no response
5. no response
6. SOX has had a profound impact on the ability of smaller public companies' management to focus on the operational needs of the company. I have several small public company clients whose entire or virtually entire management is devoted to the preparation of periodic disclosure documents. This is most noticeable during the period of the year spanning the preparation of the Annual Report on Form 10-KSB, the proxy statement relating to the Annual Meeting of Shareholders and the first quarter 10-QSB. At such times, business can literally come to stand-still. I even have solid middle-market public company clients who experience this phenomenon, which only reinforces the extreme impact on the smaller companies. My smaller public company clients have *without exception* expressed their belief that the cost-benefit analysis of the increased amount of their time that they have to direct toward compliance greatly outweighs the benefits of transparency and accountability promoted by the SOX regime. It should be noted that these companies are not criticizing SOX and its philosophy, which they also universally endorse. Rather, they are commenting on the high cost in human and financial capital to comply with SOX, which for many smaller public companies is virtually overwhelming. Compounding the problem, when these companies are extended beyond their abilities, there must be more involvement by outside counsel and others, further increasing the costs of compliance.
7. no response
8. I have not detected an increase in securities litigation among smaller public companies as a result of the current securities regulatory system. However, the first "test" cases of Enron, World Com, Adelphia, etc. are still working their way through the courts. I believe that it is too soon to tell whether or not securities litigation will become more focused on smaller public companies, who will – because of more limited resources and greater proportionate burdens – perhaps be more likely to have technical violations under the greatly enhanced current securities regulatory system, thereby exposing them to an increased threat of litigation by an activist plaintiffs' bar.
9. SOX has had a dramatic impact on the capital raising plans of smaller public companies. To be sure, it is well known that many so-called "orphan" public companies have a hard time raising capital in the best of times. Since 2003, I have extensively and scientifically studied the dollar cost of compliance under SOX for public companies, the largest individual components of which are auditing expenses, legal fees, director and officer insurance, board compensation and investor relations costs. For a small public company, the minimum estimated annual cost of being public is $500,000 and this can easily run much higher, even among "SB" filers. It must also be noted that this estimate does not include the one-time costs of SOX 404 set-up and the ongoing additional costs of 404 attestation when non-accelerated filers become subject thereto. Estimates of 404 set-up, based on current requirements, are in the six-figure range for even small public companies, and the cost of 404 attestation is estimated to run as much as the cost of the audit itself. The disproportionately high cost of being public by a smaller public

company makes such a company an even less attractive financing candidate, because of the adverse bottom-line impact to smaller profits or greater losses when corporate expenses are factored in.

10. no response
11. no response
12. no response
13. no response
14. Because SOX 404 has not yet been implemented for non-accelerated filers, it is too soon to know what the cost-benefit analysis will look like. However, I think that a scalable approach to SOX 404 compliance by smaller public companies is preferable to a total exemption. The public benefit to any public company's shareholders is met through good corporate governance and financial reporting. The issue is not the principle of compliance, but the scale, scope and cost of compliance. Even for smaller public companies, 404 set-up is estimated to cost six figures and the cost of 404 attestation is projected to equal the cost of the audit itself, not to mention the additional cost of an internal or outsourced internal controls function.
15. SOX has had a significant negative impact in the relationship between smaller public companies and their auditing firms. In my experience, anecdotally, there are far fewer discussions between management and the auditors and there is confusion on the part of management in some cases about what can even be discussed with the auditors. Additionally, I suspect that some companies' management are afraid to discuss matter openly with their auditors for fear that problems, delays and significant additional costs will result.
16. no response
17. Extending the effective dates for smaller public companies to comply with new accounting standards makes sense for a number of reasons. Firstly, it will ease, on a cash flow basis, the financial burden of compliance by smaller public companies. Secondly, the allocation of relatively scarce capital resources for such compliance can be deferred until such time as smaller public companies are certain about what their compliance requirements will look like. Thirdly, the Staff of the Commission will have more time, along with input from interested commenters, to assess to effectiveness of new accounting standards to date applicable to accelerated filers. This more measured approach will allow a more balanced regime to be developed, permit analysis of the anticipated cost of such regime, allow for a cost-benefit analysis of that regime, and give smaller public companies adequate time to budget for and implement these changes, knowing that this is the "final" version of the standards to which they will be required to adhere. I had clients who incurred expenses and time in a "false start" of 404 ramp-up during 2004 prior to the most recent deferral of 404 phase-in for non-accelerated filers. To date, I do not believe that the financial markets have been impatient with smaller public companies during the delay of implementation of the full set of accounting standards and I do not believe they will do so during the remaining pendency of that implementation. It should also be noted that many smaller public companies are "micro-cap" or "nano-cap" public companies and do not have meaningful following in the financial markets anyway, with or without SOX considerations factored in.
18. There is no question that expanding the role of the auditors to encompass more services would dramatically reduce the cost of compliance for smaller public companies. There is a fixed cost for each professional or service brought on-line by a public company, as well as a learning curve, and the fixed cost component falls disproportionately on smaller

public companies as the costs of compliance represent a significantly higher percentage of such companies' revenues. Accordingly, their higher proportional cost of compliance adversely affects the bottom line, by narrowing profit or widening loss, which could be expected to result in lower market value for their quoted or listed stock, since there is no earnings-per-share multiple "handicapping" by the financial community of a public company with a higher proportional cost of doing business.

19. The current quarterly reporting system for public companies is extremely valuable to ensure regular, periodic, material information is conveyed to the marketplace, and should be retained for the integrity of the financial markets and the protection of shareholders. A change to a less frequent full financial reporting could have a serious negative impact on stock price and the ability to complete a financing or significant M&A transaction.
20. Segment information adds considerable burden and cost to the audit or review of financial statements, as well as adding often duplicative (or overlapping) disclosure in the body of an Exchange Act report (e.g. segment reporting of results of operations in MD&A). Relief from segment reporting would be of great benefit to smaller public companies, whose real operational structures are often much simpler than segment reporting would suggest, giving an inaccurate impression of complexity of the business model.
21. no response
22. The principle burdens for smaller public companies are in attracting and retaining independent directors, because of competitive factors for qualified public company directors given their expanded role and time commitment, the increased cost of director compensation, and the cost of obtaining director and officer insurance, which sometimes is prohibitively expensive for smaller public companies (at least in terms of coverage limits that are attractive to independent directors.) In my experience, smaller public companies in many cases are floundering in trying to find enough qualified directors, including but not limited to financially literate directors. Moreover, smaller public companies often have virtually identical Board committees, because the independent directors must be "recycled" due to the typically smaller size of the board and/or the smaller number of independent directors. It would be very helpful if smaller public companies were allowed to have at least *one-third* of their boards composed of independent directors and/or a *majority* of each committee composed of independent directors. Other relief in listing requirements would be to permit smaller public companies to opt to have their Audit Committee also handle compensation matters, reducing the need for a stand-alone Compensation Committee. Other meaningful listing requirements relief would permit the governance/nominating committee be optional for smaller public companies, provided that another committee of the board, or the board as a whole, assumes these functions. Companies should be required to explain clearly their particular implementation of corporate governance relief in Part III of their 10-KSB or their proxy statement, to assure the marketplace and shareholders of full compliance with the obligations of corporate governance functions using a more flexible corporate governance structure.
23. The enhanced disclosures and shorter time frames of Current Reports on Form 8-K have proven to be a great burden to smaller public companies. This is especially true of Item 1.01 and 1.02 disclosure because of the lower standard of materiality, and Item 3.01 and 3.02 disclosure (even with the 5% threshold) because of the typical need of smaller public companies to sell unregistered securities because more traditional secondary financing is unavailable to them. If there could be a dollar threshold or other safe harbor

for materiality only for purposes of Item 8-K reporting, that would be very helpful to ease the daily burden of reporting; any such disclosure would have to be made in the next Exchange Act report on Form 10-QSB or 10-KSB. Similarly, some consideration should be given to raising the threshold for Item 3.01 disclosure, since it is not difficult for a smaller public company to exceed this from one 10-QSB to the next.

24. I have had no first-hand experience with clients concerned over the loan prohibition provisions of SOX and believe that the benefits of this provision of SOX outweigh any burden to public companies, regardless of size.
25. Small public companies have come greatly to depend upon the relief of Regulation S-B in their Securities Act filings and Exchange Act reports. However, the eligibility to use Regulation S-B should itself be reviewed, to incorporate higher revenue and/or asset and/or market capitalization tests, to expand such relief to a broader class of smaller public companies. There is no impairment of investor protection for current SB filers who comply with Regulation S-B; therefore, if only the class of companies eligible to rely on Regulation S-B were increased, without diluting the requirements of Regulation S-B itself, there should be no additional impairment of investor protection, just an increase in the number of companies who have reduced disclosure responsibility.
26. With a smaller shareholder base, the cost of printing and distributing proxy statements and annual reports is not unduly burdensome, particularly when compared to some of the other far more burdensome costs and obligations for such companies.
27. The phase-down for 10-QSB and 10-KSB reporting deadlines will be a significant burden to small business issuers. These companies are already under tremendous pressure in terms of financial resources and human capital to comply with all of their other obligations. Their systems and controls, including disclosure controls and procedures and internal controls, may require more effort to bring the company ready for filing. While not previously studied to my knowledge, I believe that a significant percentage of SB filers already file their Exchange Act reports under the extension provided by Rule 12b-25; accelerating their due dates even further will simply ensure that more such companies file under Rule12b-25 or file late as they just may not be able to get everything completed in time. For many of these companies, it is not a question of devoting greater financial and human resources to the preparation and filing of Exchange Act reports, as they just do not have the resources available. Moreover, the reality of modern American public company life is that these smaller public companies must compete for the attention of auditors and outside counsel who themselves are also burdened by shorter across-the-board filing schedules. These factors may well conspire to put a lot of SB filers out of compliance with Exchange Act filing deadlines. To the extent that late filings threaten exchange listing or OTCBB status, this is a case where the burden of implementing the next shortened set of filing deadlines significantly outweighs the benefit to the marketplace of getting public information a few days earlier, which, as noted, often doesn't happen anyway. It would be the shareholders most of all who would suffer if a company is dropped to the "pink sheets". Secondarily, "pink sheet" status severely limits financing possibilities for public companies, since many funds may not invest in "pink sheet" companies. This would be a draconian, but foreseeable outcome, of implementing further acceleration of Exchange Act filing deadlines.
28. I believe that for most smaller public companies the existing Rule 701 limits are sufficient and should not be changed.
29. no response

I thank the Committee for the opportunity to share my views on these vital issues.

Very truly yours,