

**SEC Advisory Committee
Chicago, Illinois -- August 9, 2005
by Donald S. Perkins
Chairman, Nanophase Technologies, Inc.
Romeoville, Illinois**

Good afternoon. My name is Donald S. Perkins. I am the non-executive Chairman of the Board of Nanophase Technologies, Inc. With me is Jess Jankowski, Chief Financial Officer of the company. Nanophase produces nano-size materials measured in billionths of a meter for use in sun screen and other personal care applications, semiconductor wafer polishing or to add to the wear-resistance of both paint and transparent coatings to name just a few uses.

Nanophase financed its early development by going public in 1997. Sales growth has been slower than we had expected but investor confidence in our future remains high.

Nanophase's stock multiple and related market capitalization are not reflective of its size and resources. As a high tech company in a high profile industry, our market capitalization of \$120 million represents more than 20X SALES. We have revenues in the \$5 million annual range.

We have only 50 employees. Three of these are finance and accounting professionals who are responsible for everything from entering vouchers, billing,

paying bills, cost accounting, SEC reporting, sales and franchise tax reporting, budgeting, forecasting, contract review and investor relations, among other things.

In an environment as small as ours, redundant controls are inherently inefficient. The CFO signs every check and approves every purchase order in excess of \$1,500. The CEO signs every check over \$10,000 and approves every purchase order over \$5,000. I or another Board member must approve any check exceeding \$250,000. We have seven people responsible for the administration of our small company but may soon need to add a person to accommodate the systems demanded by our auditors as part of SOX-404.

Because of the one-size-fits-all approach to SOX-404 requirements, an unwarranted and, we believe, unnecessary burden has been put on our small company. In 2004 over \$259,000 (5% of our sales) was spent and over 1000 hours were used for us to produce a SOX-404 result that showed no material weaknesses. Our 2005 costs are projected to be 2/3 of the 2004 costs. In these numbers, we have not included the tens of thousands of dollars in additional annual and quarterly fees incurred with our auditors relating to the change in the general climate since 2001 and the specific enhancements previously required by the other sections of the Sarbanes-Oxley legislation. We believe that our shareholders would be better served if those dollars and those hours were spent on revenue enhancement and new product development.

Since we disclosed the results of our SOX-404 audit in March, not a single one of our investors, many of whom are in weekly contact with the Company, has made even a passing comment regarding the completion of our 2004 SOX-404 audit with no findings of material weaknesses.

It seems to us that many small companies have investors who understand many of the risks involved and do not expect “Fortune 500-level” internal control systems to be in place.

Since we operate at a loss our SOX-404 expenditures directly reduce our sales and R & D expenditures as we build our small but promising business.

But the past is past.

Your interest is in the future and we have four suggestions for your consideration:

- 1) Use a revenue test as well as a market capitalization test for requiring SOX-404 compliance. Even a \$50 million revenue requirement would help companies like Nanophase avoid spending such a high percentage of sales on accounting. As an alternative, have a much more limited set of requirements for small companies to comply.**

- 2) **Permit, or better yet, require audit firms to do all of the work for small companies to complete whatever is required of them under SOX-404. One-fourth of our 2004 SOX-404 expense was required because our audit firm, McGladrey & Pullen told us that their interpretation of their role under PCAOB rules prohibited them from doing this work.**

We believe that our total auditing bill would have been less expensive if they had done all of the SOX-404 work. We had to contract with an outside firm to complete it. The complications and expense of time as well as money to have three of us trying to coordinate this effort was inefficient to say the least.

- 3) **(This one would help Nanophase now.) Do not require an annual reaffirmation of the internal controls of a small company like Nanophase. Let us revisit the effort every three or so years.**

4) Redefine the IT expectations for small companies.

The IT portion of the SOX-404 project was probably designed by technicians who had spent much of their careers working with banks and other institutions that have long been subject to strict control standards. Given that Nanophase operates largely on off-the-shelf software, a values clash ensued on day one. After many meetings, our auditors modified their own IT consultant's view of what was appropriate. These issues still remain partially unresolved.

Jess and I thank you for listening to our frustration and we will welcome a more reasonable approach to meeting the spirit of SOX-404 for new but small high tech companies such as Nanophase.