

WYNNEFIELD CAPITAL, INC.

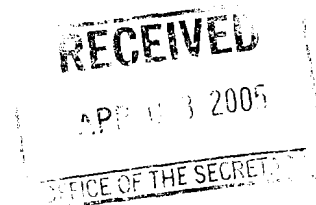
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April 7, 2005

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609



**Re: File No. 265-23
First Meeting of SEC Advisory Committee on Smaller Public
Companies**

Dear Mr. Katz:

We are writing to request that the SEC Advisory Committee on Smaller Public Companies (the "Committee") consider the needs of investors in determining ways to provide relief from Sarbanes-Oxley and other federal securities regulations and their unintended consequences. All too often, management cites Sarbanes-Oxley as the reason for a Form 15 filing that deregisters their securities under the Securities Exchange Act of 1934 (the "Exchange Act") and avoids the requirement for uniform timely reporting (ie, the Company "goes dark"). Frequently, this artifice cloaks management's real purpose – to take their company private without paying outside shareholders a fair price or avoiding potentially embarrassing governance or economic disclosures.

Many deregistrations takes advantage of an arcane loophole that allows issuers to count as "holders of record" only those shareholders who hold stock certificates in their own names and deregister when they have fewer than 300 "holders of record." Shareholders holding stock with their broker in "street name" are not counted as holders of record. As a result, many of the companies that have deregistered recently have a large number of beneficial owners of their stock, far beyond the 300 "holders of record" required under the Exchange Act. Over the past 35 years, the Commission has undertaken several initiatives to encourage investors to hold their stock with their brokers to facilitate more efficient clearing and settlement. The unintended consequence of these initiatives is that investors in smaller public companies have been subject to abusive deregistration.

Wynnefield therefore asks the Committee to place on its agenda for serious consideration the request for rulemaking under Section 12(g)(5) of the Securities Exchange Act of 1934 (the "Exchange Act") that was submitted to the Securities and Exchange Commission

are barred from holding unregistered securities, resulting in further declines in the value and liquidity of the publicly traded stock.

I am cognizant of the financial and other burdens faced by smaller public companies attempting to comply with Sarbanes-Oxley, and especially Section 404, as is the Commission. It has been my privilege to serve as a director of several smaller public companies, and as such, I am well aware of the cost of compliance with Section 404. We encourage the Committee to find ways to lessen this burden on smaller public companies.

Nonetheless, it is a sad irony that Sarbanes-Oxley, which is intended to protect investors, is frequently invoked by management to deprive investors in smaller public companies of the disclosures necessary to make sensible investment decisions. At least two academic studies produced by prestigious universities have shown that the deregistration decision is not primarily motivated by the burdens of Sarbanes-Oxley. Instead, deregistration is mostly likely to occur at an issuer where management holds a high percentage of the issuer's stock.²

Management shareholders, of course, do not require the protections of the Exchange Act to obtain useful disclosures about the issuer and its securities. That information is available at their fingertips. On the other hand, a management that plunges outside investors into the dark avoids the need to respond to troubling questions about its performance and compensation from an informed investment public. It is exactly this incentive to avoid disclosures that may reflect negatively on management performance and the resulting inequities caused by a lack of uniform disclosure that the registration requirements of the 1934 Exchange Act were meant to address.

Strengthening the Market for Smaller Public Companies

In working with smaller public companies in my capacity as a managing member of Wynnefield Capital Management, LLC, the general partner of the Wynnefield funds, over the past twelve years, I have never failed to be impressed by the vitality of this market, which functions as the great salt marsh for the nation's economy. This is the market where new ideas spawn, once-famous, but now obsolete, notions perish, and industries pronounced dead are reorganized and rise from the ashes to new life. As we are all aware, the creativity and energy of this market and all capital markets rests on a bedrock of trust between issuers and investors. This bedrock is strengthened by accurate, uniform and timely disclosure.

Wynnefield believes that continuous, uniform disclosure is a primary and fundamental obligation of public companies, particularly those that have taken advantage of the IPO process. Informed investors are willing to give management a chance to succeed with new ideas and stay the course through difficult times. Without good uniform disclosure,

² Leuz, Triantis and Wang, "Why Do Firms Go Dark? Causes and Economic Consequences of Voluntary SEC Deregistrations," November 2004 (not yet published study sponsored by Pennsylvania's Wharton School and Maryland's Robert H. Smith School of Business); Marosi and Massoud, "Why Do Firms Go Dark," July 2004 (not yet published study sponsored by the University of Alberta).

(the “Commission”) in July 2003. We are not one of the original petitioners, but have actively supported this proposal, which would close a loophole that may be used to disenfranchise investors in smaller public companies. A copy of the petition making this request is attached.

Wynnefield Capital and its related investment partnerships have been significant investors in the equities of smaller public companies for over twelve years. I have personally been actively involved with small cap investing for over 35 years.

The Abusive Use of Form 15

Recently, small cap investors have been increasingly victimized by the very troubling practice of creeping privatization. Citing the requirements of Sarbanes-Oxley, many smaller issuers of publicly traded securities have abused Form 15 by deregistering their securities under the Exchange Act.¹ After the market price declines due to the lack of information and liquidity, insiders may purchase the stock for their own account at reduced prices without any disclosure to public investors.

Deregistered issuers are immediately no longer obligated to file the uniform disclosures required in annual, quarterly and periodic reports on Forms 10K, 10Q and 8K. Management can provide any information it chooses, or no information at all; there is no uniform method used by deregistered public companies to provide information to shareholders. Management can increase its compensation and remove assets from the Company at any price internally agreed upon without disclosure to shareholders. Management is not in any way bound by the short-term profits rules that protect investors from the abusive use of inside information. The disinfecting sunlight of disclosure does not inhibit the management of deregistered issuers.

The immediate practical impact of deregistration is a fall in the market price of the issuer’s common stock. Over a longer term, the stock price generally declines because investors lack transparency and liquidity. Some companies provide token bits of financial information. However, information regarding executive compensation and other extremely useful items of disclosure that would have been available under uniform reporting rules vanish immediately for outside investors. These practical realities present a golden opportunity for management that intends to take its company private anyway to accomplish that transaction at a price that is unfair to outside shareholders.

It is important to understand that these are public companies, in the sense that investors understand the term. These are issuers of publicly traded securities, many of which trade actively. In many cases, these issuers have raised capital in initial public offerings within the recent past. Having taken the public’s money, these Form 15 filing issuers and their managements feel no responsibility to keep the investing public informed through uniform disclosure rules. Investors that maintain their holdings in these publicly traded companies are left at the mercy of managements who have already demonstrated a desire to withhold information from outside investors. Many institutions and other fiduciaries

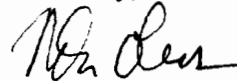
¹ Form 15 is used to deregister securities under Sections 12 of the Exchange Act.

investor interest, liquidity and willingness to hold securities collapses. The vacuum breaks the bonds of trust between issuer and investor, damaging the capital markets that have helped our country to prosper.

We urge the Committee to consider the needs of public investors for uniform disclosure in proposing solutions to the burdens presented by Sarbanes-Oxley on smaller public companies. Management should not be able to use Sarbanes-Oxley as a subterfuge that frequently deprives shareholders from achieving fair value for their investment. In particular, we ask the Committee to examine the inequities produced by the arcane "holder of record" definition of Rule 12g5-1 under the Exchange Act, and recommend a new rule to protect investors.

We would appreciate the opportunity to make a personal presentation describing our own experiences as an investor in smaller public companies and to provide any other information that the Committee would find helpful in its deliberations. You can reach me at (212) 760-0134.

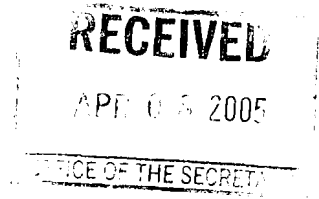
Sincerely,



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July 3, 2003

Mr. Jonathan Katz
Secretary
United States Securities and Exchange Commission
450 5th Street, N.W.
Washington, D.C. 20549

**Re: Petition for Commission Action to Require Exchange Act
Registration of Over-the-Counter Equity Securities**

Dear Mr. Katz:

On behalf of David Shuldiner of Kanagawa Holdings LLC, Walter P. Carucci of Carr Securities Corporation, Paul H. O'Leary of Raffles Associates, L.P., Paul D. Sonkin of Hummingbird Management LLC, David Cohen of Athena Capital Management, David W. Wright of Henry Investment Trust, L.P., James E. Mitchell of Mitchell Partners, L.P., Jack Howard of Steel Partners, and Matt Brand of Performance Capital Group, LLC, each of whom are well-respected institutional investors (collectively, the "Institutional Investors"), The Nelson Law Firm, LLC respectfully petitions the Securities and Exchange Commission (the "Commission") to take immediate action to protect investors and prevent inequitable and unfair practices in the over-the-counter markets. In particular, the Institutional Investors request that the Commission exercise its authority under Section 12(g)(5) of the Securities Exchange Act of 1934 (the "Exchange Act") to amend Rule 12g5-1 under the Exchange Act ("Rule 12g5-1") to include as "held of record" with respect to any particular equity security each account for a beneficial owner holding the security in "street name." The proposed amendment (the "Beneficial Owner's Rule") is attached hereto as Exhibit A.

The Beneficial Owner's Rule will (i) conform a 38-year old rule to modern clearing practices, (ii) serve the public interest and further the objectives of Section 12 of the Exchange Act by requiring accurate, public reporting by issuers with many shareholders and (iii) prevent the current widespread manipulation of the capital markets by some unprincipled issuers.

Introduction.

In response to complaints about fraudulent activity by companies with equities trading in the over-the-counter markets, Congress enacted legislation in 1964 to require a company having total assets in excess of \$10 million and a class of equity securities

held of record by 500 or more persons to file a registration statement under the Exchange Act.¹ Companies whose record holders thereafter declined beneath 300 holders of record, or 500 holders of record and total assets less than \$10 million, would be permitted to deregister. As a practical matter, the legislation, which added a new Section 12(g) to the Exchange Act, for the first time required companies issuing securities that are traded over-the-counter to provide the information generally available to investors in securities listed on the New York Stock Exchange. Over-the-counter companies registered under Section 12(g) also were required for the first time to comply with the proxy rules and insider trading and reporting requirements of Sections 14 and 16 of the Exchange Act.

Section 12(g)(5) of the Exchange Act granted authority to the Commission to promulgate rules defining the meaning of the term "held of record". The Commission responded by proposing a new Rule 12g5-1 in 1964. This proposed rule was adopted in its current form in 1965.

Rule 12g5-1, as initially proposed, would have required each account held in "street name" to be counted as "held of record."² An issuer would have been entitled to rely in good faith on the representations made by the broker-dealer or bank concerning the number of accounts holding securities in street name. In response to numerous comments from brokerage industry participants who complained that Rule 12g5-1 as proposed would be too burdensome, the Commission dropped the requirement to count each account held in "street name" as "held of record". Instead, the Commission required issuers to count as "held of record" only those shareholders listed on the corporate records who had been issued a stock certificate.

For reasons that are not entirely clear, the Commission imposed a different requirement on foreign issuers. Exchange Act Rule 12g-3(a)(1) requires foreign private issuers to count each account held in street name by a broker or bank to determine whether their stock must be registered because it is held of record by more than 300 US investors.³

¹ The Act, as adopted by Congress, required Companies with 500 shareholders and total assets greater than \$1 million to register under the Exchange Act. Amendments adopted as Exchange Act Rule 12g-1 pursuant to the Commission's authority under Section 12(g)(5) of the Exchange Act have raised the "total assets" threshold to \$10 million. These amendments were intended to effectuate Congressional purposes by taking account of inflation.

² SEC Release No. 34-7426 (1964). The proposed rule contained a paragraph (b)(3) which provided as follows: "To the extent indicated below, securities registered in the name of a broker, dealer or bank or nominee for any of them, which at the time are being held by the broker or dealer in customers' accounts or by the bank in custody or investment advisory accounts, shall be included as held of record by the number of separate accounts for which the securities are held. Each registered owner known by the issuer, or a person maintaining its record of security holders, to be a broker, dealer or bank or nominee for any of them shall be requested to furnish the issuer the number of such separate accounts. A recipient of such a request will be expected to comply only to the extent the information can be readily supplied, and the issuer may rely in good faith on such information as is received in response to the request."

³ Exchange Act Rule 12g3-2(a)(1) provides as follows: "Securities of any class issued by any foreign issuer shall be exempt from Section 12(g) of the Act if the class has fewer than 300 holders resident in the United States. This exemption shall continue until the next fiscal year end at which the issuer has a class of equity securities held by 300 or more persons resident in the United States. For the purpose of

There is no evidence to suggest that this requirement for foreign private issuers has imposed an undue burden on either issuers or the banks and brokerage firms that have been required to respond to such requests.

The contrasting treatment for US domestic issuers and foreign issuers under the rules adopted pursuant to Section 12(g)(5) of the Exchange Act produces inconsistent and perverse results. Investors in US issuers are deprived of the disclosures and protection provided under the Exchange Act to investors in foreign companies.

The 38 years since Rule 12g5-1 was adopted have witnessed monumental changes in clearing and settlement procedures. The transformation of clearing and settlement procedures have caused, among many other things, a dramatic increase in the percentage of beneficial owners holding equity securities in street name. In contrast to conditions that prevailed in 1965, it is now unusual for a beneficial owner to appear on the corporate books as a holder of record or hold a stock certificate. As a result, Rule 12g5-1 fails to properly effectuate the Congressional intent expressed in Section 12 or the policy goals of the Exchange Act.

This petition contains four parts. In the first section, we describe recent illustrative examples of companies that have used the definition of "held of record" in Rule 12g5-1 to avoid their duties to investors under the Exchange Act. The second section points out the harsh consequences of the rule's application on the investing public. The third section demonstrates that the definition is obsolete and no longer aligns with modern clearing practices. Finally, we will show that adopting the Beneficial Owner's Rule as proposed will not impose burdensome requirements on companies or the brokerage industry. Rules adopted in response to the Shareholder's Communications Acts have led to the development of an efficient industry procedure easily accessed by companies at nominal cost to determine the correct number of beneficial owners who should be counted as record holders.

Commenting on its decision not to require inclusion of street names in determining the number of accounts "held of record", the Commission noted that it would "determine in the light of experience whether inclusion of these accounts at a future date is necessary or appropriate to prevent circumvention of the Act and to achieve the intended coverage on a uniform and acceptable basis."⁴ We submit that recent experience provides strong and persuasive evidence that inclusion of these accounts is essential to prevent widespread circumvention of the Exchange Act and to protect the investing public.

determining whether a security is exempt pursuant to this paragraph, securities held of record by persons resident in the United States shall be determined as provided in Rule 12g5-1 except that securities held of record by a broker, dealer or bank or nominee for any of them in the United States for the accounts of customers resident in the United States shall be counted as held in the United States by the number of separate accounts for which the securities are held. The issuer may rely in good faith on information as to the number of such separate accounts supplied by all owners of the class of its securities which are brokers, dealers or banks in the United States or a nominee for any of them."

⁴ SEC Release No. 34-7492 (1965).

Recent Examples of Circumvention.

In the very recent period beginning in January 2003, we have identified 24 issuers that have deregistered their securities under circumstances suggesting manipulation of the capital markets and circumvention of the Exchange Act.⁵ The following discussion will focus on three examples that are illustrative of the current abusive practices perpetrated by issuers whose securities are traded on the over-the-counter markets.

SmartDisk Corporation – Using the Capital Markets as a Personal Piggybank.

On May 7, 2003, SmartDisk Corporation (NASDAQ: SMDK) filed a Form 15 with the Commission to deregister its common stock and suspend its reporting and disclosure obligations under the Exchange Act on the grounds that it has less than 300 “holders of record.”⁶ In a press release, SmartDisk complained about the costs associated with preparing and filing periodic reports with the Commission.⁷ The facts suggest a more sinister motive.

On October 5, 1999, SmartDisk sold 3 million shares of its common stock to the public at a price of \$13.00 per share. Of the \$39 million raised from public investors, SmartDisk received \$36,270,000 after paying all costs of the transaction. This offering was a significant achievement for a technology company with one product, a device used to transfer digital photographs to computers only from Toshiba cameras, and that had only been in business for little more than a year.⁸

In its first annual report for the year ended December 31, 1999, SmartDisk disclosed that over 16 million shares of its common stock were outstanding with over 1,000 beneficial owners. The vast majority of these shares were held in street name. Accordingly, the corporate books showed only 76 “holders of record.” SmartDisk’s stock price had traded in a range from \$23.44 to \$55.19 per share.

In late Spring of 2000, SmartDisk sought to capitalize on its earlier capital-raising success, and the trading interest in its common stock, by launching another public offering, this time attempting to obtain \$133,568,907 from public investors.⁹ By mid-2000, however, the public’s appetite for investment in unproven technology companies

⁵ Exhibit B provides pertinent information regarding these issuers.

⁶ SEC File No. 000-27257 (2003).

⁷ SmartDisk cited the following reasons for its decision to deregister: (i) the market value that the public markets are applying to the Company, (ii) the costs, both direct and indirect, associated with the preparation and filing of the Company’s periodic reports with the SEC, (iii) the expected substantial increase in costs associated with being a public company in light of new regulations promulgated as a result of the Sarbanes-Oxley Act of 2002, (iv) the fact that the Company’s stock is very thinly traded, (v) the nature and extent of the trading in the Company’s common stock, and (vi) the lack of analyst coverage and minimal liquidity for the Company’s common stock.

⁸ SEC File No. 333-82793 (1999). SmartDisk, a company located in Naples, Florida, was incorporated in Delaware on March 5, 1997 as “Fintos, Inc.” and changed its name to “SmartDisk Corporation” on September 26, 1997. Significant operations related to its then current products were commenced in January 1998, and SmartDisk received its first significant capital contributions in May 1998.

⁹ Registration Statement on Form S-1. SEC File No. 333-35300 (2000).

had diminished, and SmartDisk was forced to withdraw its proposed offering. SmartDisk was, however, successful in registering the stock of insiders holding SmartDisk common stock, who unloaded 1,576,768 shares to the public for a total offering price of \$8,672,224.

In September 2002, SmartDisk again sought to raise capital from public investors, this time through a rights offering for the more modest amount of \$7,500,000.¹⁰ The company's stock price had now fallen to \$.16 per share. Again, market conditions forced the company to withdraw this offering.

In its fourth annual report for the year ended December 31, 2002, SmartDisk disclosed that 17,790,770 shares of its common stock were outstanding. The company estimated that its stock was now held by more than 6,000 beneficial owners, most in street name. 165 "holders of record," more than twice the number identified after the company's initial public offering, appeared on the corporation's books.

SmartDisk has over 6,000 public investors, who have entrusted to this company's management over \$36 million. Ignoring the responsibilities incumbent on such trust, SmartDisk's management spurns its duty to communicate with investors. Instead, it only cares about taking their money. When the public's investment interest was at its peak, SmartDisk was only too happy to access the public markets to finance its ideas. In these times, when capital-raising is difficult for technology companies with little or nothing in the way of earnings, SmartDisk's management would callously plunge over 6,000 public investors into the dark, depriving them of the ability to monitor the management of the \$17 million in total assets remaining from their original investment.

We submit that the Exchange Act was never intended to operate as a vehicle for fair weather disclosure by issuers. Issuers should not be entitled to treat the public capital markets as a personal piggy bank, providing public disclosures when capital-raising opportunities are abundant, but then shutting off the lights when Exchange Act registration becomes inconvenient. This practice is an abuse of trust that persists unchecked because existing Rule 12g5-1 is obsolete. The management of SmartDisk and other over-the-counter companies eagerly exploit this loophole.

United Road Services, Inc. – Viewing Registered Equity as Acquisition Currency.

Without fanfare or comment, United Road Services, Inc. (OTCBB: URSI) filed a deregistration statement on Form 15 on May 14, 2003.¹¹ United Road Services provides an example of an issuer who views its common stock as "acquisition currency," jettisoning its disclosure obligations to investors when the currency is devalued.

United Road Services is a national provider of motor vehicle and equipment towing, recovery and transport services, operating 79 facilities in 25 states. Its clients include

¹⁰ Registration Statement on Form S-1. SEC File No. 333-67022 (2002).

¹¹ SEC File No. 000-24019 (May 14, 2003).

leasing and insurance companies, car dealers, law enforcement agencies, auto auction companies, and individual drivers.¹²

The business of United Road Services was launched through an initial public offering in May 1998, during the home stretch of the great bull market, when it sold 6.6 million shares to public investors at a price of \$13.00 per share, thereby raising \$85.8 million.¹³ United Road Services immediately used this capital to purchase seven major towing companies. Over the next year, United Road Services acquired 49 additional companies. The Company made its last acquisition on January 16, 2002. Most of these acquisitions were paid for with stock.¹⁴

The acquisition policy of United Road Services has not proven to be particularly profitable. Consequently, the Company's stock is currently traded at around 5 cents per share. However, United Road Services still shows \$97,767,000 in total assets. There are 294 holders of record for United Road Services' common stock. While information regarding the number of beneficial owners is not publicly available, we believe that this Company's common stock is beneficially owned by over 6,000 shareholders.

At the current trading price, the stock of United Road Services is no longer useful for acquisitions. Having exploited its value fully, this Company's management would now turn its back on its disclosure obligations to shareholders, relying on the obsolete Rule 12g5-1 definition to deregister its stock. Many of these shareholders received some of this Company's "acquisition currency," in exchange for their company's assets. It is a cruel result, and contrary to purposes of the Exchange Act, to deprive them of their last remaining good opportunity to influence the management of their hard-earned investment dollars.

ACAP Corporation – Sharing Risks, But Not Rewards, with Public Shareholders.

ACAP Corporation filed its deregistration statement on May 14, 2003,¹⁵ at which time it had 241 holders of record. While beneficial ownership information is not publicly available, we believe that this record ownership represents over 500 public shareholders. ACAP holds \$146,799,869 in total assets.¹⁶ ACAP is the story of a successful company, determined not to share its abundant wealth with the shareholders responsible for its profitability.

ACAP is a life insurance holding company, formed in 1985 to become the parent of American Capitol Insurance Company. American Capitol is a Texas life insurance

¹² Annual Report on Form 10K for the period ended December 31, 2002. SEC File No. 000-24019 (April 15, 2003).

¹³ Registration Statement on Form S-1. SEC Registration Statement No. 333-4692 (1998).

¹⁴ *Infra*, note 11.

¹⁵ ACAP Corporation, Securities Registration Termination on Form 15-12G, dated May 14, 2003, SEC File No. 000-14451 (2003).

¹⁶ ACAP Corporation, Annual Report on Form 10-KSB for the period ended December 31, 2002, SEC File No. 000-14451 (2003).

company licensed in 34 states and the District of Columbia. 45% of ACAP's stock is owned by InsCap Corporation.¹⁷

Earlier this year, ACAP decided it no longer wished to share its fairly generous returns with public shareholders. Buying out minority shareholders is not illegal. The Exchange Act provides a well-developed process for self-tendering transactions that we believe results in a fair exchange for investors. The methods used by ACAP to "go private," however, strike us as the sort of behavior the Exchange Act was intended to prevent.

Rather than making an offer to buy out the minority interest through a self-tendering transaction, ACAP decided to use its corporate power to cause a reverse split, thereby reducing the number of its outstanding shares. Fractional shares that resulted from the reverse split were purchased for cash, thereby reducing the number of "holders of record."¹⁸ This device worked, and the many remaining public shareholders of ACAP, rather than receiving fair consideration for their shares, are now being plunged into the darkness of holding shares in a Company without disclosure obligations under the Exchange Act.

In a statement typical of the attitude of issuers that twist Rule 12g5-1 to evade their obligations to long-term investors, the Board of Directors noted as a reason for the reverse split that ACAP had not used the Company's common stock to raise capital or make acquisitions for many years.¹⁹ This view that equity is only good for capital raising or acquisition currency denies the important role that public shareholders play in guiding the use of capital investment and using Exchange Act disclosure to supervise the hand of management.

The Harsh Results of Deregistration.

It is certainly true that many issuers view disclosure to shareholders as a burdensome nuisance – that is why it was necessary for Congress to mandate periodic disclosure in the Exchange Act. In addition, Sarbanes-Oxley has imposed additional requirements that in some respects increase the effort involved in making adequate disclosure.

We nonetheless submit that the wholesale termination of periodic disclosure for thousands of investors frustrates the purposes of the Exchange Act and fails to provide appropriate relief where warranted. The Commission has responded to the needs of small companies and their investors with small business initiatives tailoring disclosure obligations to their special circumstances. If additional relief is warranted, this can best be accomplished through amendment to these small business initiatives.

If the Commission approves the deregistration of SmartDisk, United Road Services and ACAP, as expected, as well as the other public companies listed in Exhibit B, the

¹⁷ See Note 15, *infra*.

¹⁸ ACAP Corporation, Information Statement on Schedule 13E-3, dated May 14, 2003, SEC File No. 005-49858.

¹⁹ See Note 18, *infra*.

disinfecting benefits of public disclosure will no longer enlighten these issuers' footsteps. Resources will no longer be dedicated to satisfy the demands of generally accepted accounting principles, leading to undisciplined business practices. Investors will no longer receive the proxy statements mandated by Section 14 of the Exchange Act that have enabled them to accurately evaluate the efforts of management and use that knowledge to make informed decisions in the election of their directors.

No longer confronting the scrutiny of informed investors, management may feel secure in its tenure, to the detriment of the thousands of public investors who can no longer rely on the federal securities laws to protect them from invidious or incompetent management behavior. Without the discipline imposed by public investors, scarce resources are unlikely to be applied by management to their most desirable uses, spreading negative consequences throughout the economy in derogation of the public interest.

Without adequate financial information to satisfy the requirements of Exchange Act Rule 15c2-11, market makers may no longer make two-sided quotes in deregistered issues. Public customers may ask market makers to find a buyer for them, but without a two-sided market, valuations amount to dubious approximations. Uncertain values make it difficult for institutional investors acting as fiduciaries to account properly for beneficial positions, resulting in liquidations at prices well below fair value.

Deprived of the good information required by the periodic reporting mandates of the Exchange Act, the public markets will trade the stock of these deregistered issuers on the basis of rumor, innuendo and uncertainty. Volatility will increase. Insiders may no longer feel inhibited by the rigors of Section 16 of the Exchange Act from taking advantage of the information they received in their positions of trust as corporate fiduciaries. Unfair informational advantages and volatile trading markets are the ingredients that enable the unscrupulous to shear shareholders of the remaining value left in their investments.

We respectfully petition the Commission for relief from this injustice inflicted on the nation's public shareholders.

The Definition of "Holders of Record" is Obsolete.

Holder of Record Meant Beneficial Owner When Rule 12g5-1 Was Adopted.

A "holder of record" is established on the corporate books when a corporation issues a stock certificate to a particular person, registering the name of that person on the stock certificate and the corporate books. In 1964, when Congress enacted Section 12(g) of the Exchange Act, most equity securities were registered to their beneficial owners on the corporate books.²⁰ A relatively small percentage of equity securities were registered

²⁰ In 1982, long after the creation of securities depositories and book-entry settlement, the ratio of book-entry deliveries to certificate withdrawals was 2.3:1. In 1992, the ratio had increased six times to 12.9:1. See U.S. Securities and Exchange Commission, 1993 Annual Report (1994) at 125. If we assume that

in the name of the broker, or in “street name,” generally when stock was being held as security for margin. Over-the-counter equities in 1964 were generally not marginable.

Accordingly, when Congress enacted Section 12(g) in 1964, determining that it was in the public interest for companies with more than 300 record holders to register under the Exchange Act, 300 record holders would be reasonably equivalent to 300 beneficial owners. We contend, for reasons that will be described later, that Congress used the term “holder of record” to simplify the process for companies trying to determine whether or not they were required to register under the Exchange Act. In 1964, among other things, there was no good way to discover the number of beneficial owners represented by street names. Since the numerical difference was unlikely to be material, there was little to be gained by imposing the burden of obtaining a completely accurate count on a few relatively small issuers.

Congress nevertheless anticipated that the term “holder of record” might not achieve its intended purpose – to mandate periodic disclosure for issuers with more than 300 shareholders – over time. Accordingly, Congress granted to the Commission authority in Section 12(g)(5) of the Exchange Act “to define by rules and regulations the [term] “held of record” as it deems necessary or appropriate in the public interest or for the protection of investors in order to prevent circumvention of the provisions of this subsection.” Exchange Act Rule 12g5-1 was promulgated in 1965 pursuant to the Commission’s authority under Section 12(g)(5).

Soon after Rule 12g5-1 was adopted in 1965, a clearing and settlement crisis erupted on Wall Street. Significant changes in clearing and settlement systems were prompted by this crisis, which caused a radical increase in the percentage of stock ownership represented by street names. These changes, which have continued over the 38 years since Rule 12g5-1 was adopted, have inexorably led to a vast disparity between the number of record holders and the number of beneficial owners. The number of “holders of record” on the corporate stock records no longer reasonably approximates the number of beneficial owners. This disparity frustrates the Congressional intent expressed in Section 12(g) of the Exchange Act and provides grist to the mill for unscrupulous managers of certain over-the-counter companies. The time has come for the Commission to re-examine Rule 12g5-1 and redefine “held of record” in the public interest and for the protection of investors.

the ratio of beneficial owners to street names is roughly equivalent to the ratio of book-entry deliveries to certificate withdrawals, then a company in 1992 with 25 holders of record would have 300 beneficial owners. This ratio has undoubtedly increased since 1992. By comparison, based on the same assumptions, a company with 300 holders of record in 1982 would have 690 beneficial owners. Significant changes in clearing practices that occurred in the early 70’s caused a “dramatic” increase in the number of accounts holding in street names. So, it is a fair assumption that in 1965 the number of holders of record for most over-the-counter issues would be roughly equivalent to the number of beneficial owners.

Changes in the Clearing and Settlement Systems Since 1965.

That Rule 12g5-1 is obsolete becomes readily apparent upon brief reflection on the modern history of trading, clearing and settlement practices. In 1965, NASDAQ did not exist. Neither The Depository Trust Company (DTC), nor its predecessor, the Central Certificate service, had been invented. Computers were a recent innovation, and only a few very large firms were experimenting with computerized bookkeeping using large main frame machines. Most recordkeeping on Wall Street was accomplished using paper ledgers, envelopes marked to indicate ownership, and file cabinet systems.²¹

In 1965, when Rule 12g5-1 was adopted, most clearing and settlement transactions involved a four-step process. To sell stock on an exchange, the beneficial owner would deliver a stock certificate together with stock powers to a broker. The broker would then deliver (generally by a runner) the stock certificate to the broker used by the purchaser. The purchasing broker would deliver the certificate to the purchaser who, in turn, would submit the certificate, along with attached stock powers, to the transfer agent for registration. This process involved multiple re-registrations on the books of transfer agents (who maintain the lists of corporate "holders of record") and was cumbersome and costly.

In 1968, this system for clearing and settling securities transactions disintegrated into chaos. Volumes on the New York and American Stock Exchanges exploded, and responding to an increased interest in over-the-counter issues, the NASD began development of NASDAQ. Stock transfer departments were overwhelmed by the increased volumes and began to fall behind. Delays at one firm held up the work at other firms who were waiting to receive stock certificates. Errors were generated causing more work; certificates were lost or stolen. By December 1968, unsettled trades had accumulated to \$4 billion and "the trade settlement system had virtually broken down."²² This "paperwork crisis," which lasted until 1971, was described in the resulting Congressional hearings as "the most prolonged and severe crisis in the securities industry in 40 years."²³

The main culprit of the "paperwork crisis" was generally agreed to be the "stock certificate." An influential report by Lybrand, Ross & Montgomery, for example, concluded that the "stock certificate [was] a chief catalyst of the paper crisis that in 1968 brought Wall Street to the edge of chaos."²⁴ When the elimination of stock certificates

²¹ For an interesting discussion of clearing and settlement practices in the 1960's see Hazen and Markham, 23 *Broker-Dealer Operations Under Securities and Commodities Law*, "Broker-Dealers – The Regulatory Era; The 60's – the Go-Go Years" § 2.14 (2002).

²² James Burk, *Values in the Marketplace: The American Stock Market Under Federal Securities Law* 106 (1988), as quoted in Hazen and Markham, *infra* n. 21.

²³ Securities Processing Act, Hearings Before the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce on H.R. 14567, H.R. 14826 and S.3876, 92d Cong. 2d Sess. 2 (1972), as quoted in Hazen and Markham, *infra* n. 21.

²⁴ Lybrand, Ross Bros. & Montgomery, *Paper Crisis in the Securities Industry: Causes and Cures, Is the Stock Certificate Necessary?* 1 (1969) (Preliminary Draft), Reprinted in, *Studies of the Securities Industry*, Hearings Before the Subcommittee on Commerce and Finance of the Committee on Interstate and

proved to be politically unfeasible,²⁵ the securities industry, with the strong encouragement of the Commission and Congress, began searching for ways to immobilize the stock certificate.

The immobilization of stock certificates has largely been accomplished through the use of street names and the creation of securities depositories. In 1968, the New York Clearing Corporation, a subsidiary of the New York Stock Exchange, established the Central Certificate Service, which was ultimately succeeded by The Depository Trust Company (DTC), using a system that has continued to date. Under this system, investors are strongly encouraged to leave their certificates in an account maintained by a broker-dealer.²⁶ In turn, broker-dealers maintain accounts at DTC, indicating the total number of shares held for their customers' accounts. To execute a delivery, the selling firm instructs DTC to debit its account for the amount of the sale and credit the buying broker's account.²⁷ Title to the shares is transferred by computer entries, eliminating the necessity of physical transfer of the certificate from customer to broker, broker to broker, and broker to customer.

The use of securities depositories has not entirely eliminated the use of paper certificates. Instead, a paper certificate representing equity ownership on the corporate books remains in place as a "global certificate" with DTC's nominee, CEDE & Co., as the "holder of record", representing all of the shares held in accounts of the brokerage firm members of DTC. These global certificates gather dust in a vault in the Wall Street area. In turn, the accounts of the brokerage firm members of DTC represent ownership by the many beneficial owners of those securities who are clients of the brokerage firms. Stock certificates are immobilized because the "global certificate" never moves from the vault.

Holder of Record Now Means Street Name.

The immobilization of stock certificates has eliminated the prior function of stock certificates to identify beneficial owners as "holders of record." In contrast to conditions in 1965, beneficial owners are no longer represented in the vast majority of cases as

Foreign Commerce, 92d Cong. 1st Sess. Ser. No. 92-37C, pt. 4, 2159 (1971), as quoted in Hazen and Markham, 23 Broker-Dealer Operations Under Securities and Commodities Law, "Clearing and Settlement. Clearing Agencies Evolve." § 3.3 (2002).

²⁵ UCC Article 8, adopted by every State, for the most part mandates the use of paper certificates because perfection is accomplished in negotiable instruments through physical possession.

²⁶ Brokerage firms penalize investors who wish to take physical possession of a stock certificate by charging a fee, usually \$50 for each transfer. In addition, investors are warned that sales will take longer to accomplish because the broker must take physical possession of the certificate, and physical possession of a stock certificate is dangerous, as the certificate can be stolen or forged. As a result, stock certificates have become a curiosity – many younger investors have only seen them in museums.

²⁷ The textual description is a bit of an oversimplification for the sake of clarity. Since the early 1990s, there have been further advances in clearing and settlement procedures with the implementation of continuous net settlement. In general, the selling firm no longer settles directly with the purchaser, but instead with the National Securities Clearing Corporation (NSCC), an affiliate of DTC, which acts as a central clearing counterparty. In turn, the purchasing firm settles with NSCC. This avoids any settlement delays caused by the failure of a single firm to deliver.

“holders of record”.²⁸ Instead, beneficial owners are represented almost entirely on the corporate books by “CEDE & Co.,” the nominee for banks and brokerage firms with accounts at DTC, and other nominee names serving similar function under other clearing systems.

There have been several attempts to create systems that would cause beneficial owners to be registered electronically as holders of record on corporate books. Most recently, the Commission in 1995 studied and approved a pilot project that would list beneficial owners electronically on corporate records through a transfer agent operated book-entry registration system.²⁹ If this pilot, known as “DRS,” had been successful, this petition would not have been necessary. As of this time, however, no good alternative has been found to replace the convention of using “CEDE & Co.” and other street names to represent the beneficial ownership of the vast majority of equity investment. Instead, the Commission’s efforts to shorten settlement cycles from T+5 to T+3 resulted in an intense investor education effort led by the Securities Industry Association to increase the percentage of investors holding their securities in street name. Further efforts to reduce settlement cycles can be expected to virtually eliminate individual possession of stock certificates.

It is submitted that at this time very few investors hold stock certificates registered in their names. Instead, their stock is held in street name by their brokerage firms. Moreover, there has been a significant increase in investor interest in over-the-counter securities in recent years. These investors assume that the protections of Section 12(g) of the Exchange Act are available to them if the stock they own is widely held. A stock beneficially owned by thousands of investors can never be considered a closely-held investment. Existing Rule 12g5-1 simply no longer conforms to common understanding and therefore presents a trap for all but the most sophisticated and legally prescient investors.

Determining the Number of Beneficial Owners is Not Burdensome.

As noted earlier, the Commission in 1965 dropped the requirement to count each account held in “street name” as “held of record” under Rule 12g5-1 in response to numerous comments from industry participants who complained that this requirement would be too burdensome. This complaint was dubious even in 1965. Foreign issuers have been required to include accounts held in street name as “holders of record” for many years without apparent difficulty.³⁰ But, to the extent that determining the number of beneficial owners was ever a burden, modernization of the proxy rules in the 1980s has resulted in a streamlined, inexpensive process to count beneficial owners holding securities in street name.

²⁸ As noted by the Circuit Court of Appeals: “Modernization of this task has led to storage of most stock certificates in a depository affiliated with the clearing agency. Thus, ‘delivery’ amounts to a bookkeeping entry that removes the security from one account and places it in another.” *Bradford Nat. Clearing Corp. v. Securities and Exchange Commission*, 590 F.2d 1085 (D.C. Cir. 1978).

²⁹ See Transfer Agents Operating Direct Registration System, Concept Release, SEC Release No. 34-35038 (1995).

³⁰ See Note 3, *infra*, and the associated textual discussion.

This process resulted from the enactment of a series of Shareholders Communications Acts beginning in 1985. The Acts reflected Congressional concern that, while the development of securities depositories solved the “paperwork crisis,” the use of street names to immobilize paper certificates erected a barrier to communication between companies and their shareholders.³¹ The Shareholders Communications Acts led to the adoption of rules for the solicitation of proxies under Section 14 of the Exchange Act. Accordingly, Rule 14b-1(b)(1)(i) requires each broker-dealer to respond within seven days after it has received an inquiry from a company that wishes to solicit proxies from the beneficial owners of its securities by indicating the approximate number of its customers who are beneficial owners of the company’s securities. Rule 14b-2(b)(1)(A) requires a similar response from banks holding their customer’s securities in street name.

The securities industry responded by developing a streamlined process for issuers to obtain information about the number of beneficial owners holding their equities.³² To solicit proxies or for any other reason, any issuer can submit a request to ADP Proxy Services and for a nominal cost immediately receive a current count of the number of its beneficial owners. We believe that issuers can use the same medium to determine whether their equities are held by more than 300 beneficial owners prompting an obligation to register and make periodic reports under the Exchange Act.

The Proposed Beneficial Owner’s Rule.

The proposed Beneficial Owner’s Rule would require issuers to use the process developed under the proxy rules to determine the number of securities “held of record” under Rule 12g5-1.

Under the proposed Beneficial Owner’s Rule, Rule 12g5-1 under the Exchange Act would be amended to provide that each beneficial owner of a security held in street name is to be counted for determining the number of securities “held of record” for the purpose of determining whether an issuer is subject to the provisions of Section 12(g) and 15(d) of the Exchange Act. An issuer would be required to inquire of each record holder of its equity securities that is a broker-dealer or bank whether other persons are the beneficial owners of such securities, and if so, the number of such beneficial owners. The issuer would also be required to inquire if such record holder holds the

³¹ As noted in the Commission’s seminal study of this issue in 1975, “[street names place] one or more layers between issuers and the beneficial owners of their stock which may make issuer-shareholder communications more difficult and expensive. The street or nominee names reflected on the issuers’ books as owners of record are not the beneficial owners, that is the persons entitled to receive dividends, vote on matters presented to stockholders, dispose of the stock or otherwise exercise the prerogatives of ownership. If the record owner is not the beneficial owner, the issuer cannot contact the beneficial owner directly, nor can the beneficial owner directly exercise the prerogatives or receive the benefits of ownership. Both must act through one or more intermediaries -- the brokerage firm or financial agent, and perhaps the depository.” Street Name Study, SEC Release No. 34-11707 (1975).

³² See Bloomenthal, *Going Public and the Public Corporation*, “Proxy Solicitations and Contests,” § 11.07 (2001).

issuer's securities on behalf of any respondent bank, and if so, the name and address of each such respondent bank. Conforming amendments would also be made to Rules 14b-1(b)(1)(i) and 14b-2(b)(1)(A) to require broker-dealers and banks to respond to inquiries from issuers made in accordance with Rule 12g5-1. As a practical matter, the requirements of the proposed Beneficial Owner's Rule can be easily accomplished through inquiry to ADP Proxy Services using the well-developed procedure under the proxy rules.

Conclusion.

We respectfully submit that the light of experience calls out for a re-examination of Rule 12g5-1. The Rule is obsolete and no longer achieves its intended purpose. The inconsistent protections provided to investors in foreign issuers over domestic issuers can no longer be justified as a matter of policy. Over-the-counter companies in record numbers are using an arcane definition to circumvent the Exchange Act and deprive the investing public of the benefits of full and accurate disclosure promised by the federal securities laws.

The Commission has authority under Section 12(g)(5) of the Exchange Act to define by rules and regulations the term "held of record" as it deems necessary or appropriate in the public interest and for the protection of investors and to prevent circumvention of Section 12(g) of the Exchange Act. We urge the Commission to adopt the proposed Beneficial Owner's Rule or, alternatively, another rule that would better serve the public interest and effectuate Congressional intent.

Please call me if you have any questions.

Respectfully submitted,

/s/ STEPHEN J. NELSON

Stephen J. Nelson

cc: Chairman William H. Donaldson
Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Cynthia A. Glassman
Commissioner Harvey J. Goldschmid
Mr. Allan L. Beller, Director of the Division of Corporation Finance
Mr. Martin Dunn, Deputy Director of the Division of Corporation Finance
Ms. Annette Nazareth, Director of the Division of Market Regulation

Proposed Beneficial Owner's Rule

Section 12g5-1 under the Securities Exchange Act of 1934 (the "Exchange Act") is hereby amended as follows:

A new paragraph (b)(3) is added to read as follows:

"For purposes of this paragraph (b)(3), the terms "entity that exercises fiduciary powers", "record holder" and "respondent bank" shall have the meanings assigned to such terms in rule 14a-1 under the Exchange Act. Each beneficial owner of securities for which a broker, dealer, bank, association or other entity that exercises fiduciary powers in nominee name or otherwise is the record holder shall be included as "held of record" by such beneficial owner. An issuer shall inquire of each such record holder: (A) whether other persons are the beneficial owners of such securities and if so, the number of such beneficial owners and (B) whether it holds the issuer's securities on behalf of any respondent bank and, if so, the name and address of each such respondent bank."

Paragraph (b)(3) is renumbered (b)(4).

Rule 14b-1(b)(1) is amended to insert the words "Rule 12g5-1(b)(3)," after the word "with" and before the words "Rule 14a-13(a)".

Rule 14b-2(b)(1)(i) is amended to insert the words "Rule 12g5-1(b)(3)," after the word "with" and before the words "Rule 14a-13(a)".

**Companies Deregistering to Circumvent the Exchange Act
In 2003**

- 1. SEMX Corp, 1 Labriola Court, Armonk, NY 10504 (telephone: (914) 698-5353). Holders of Record: 89. Estimated Beneficial Owners: 1,800. Total Assets: \$30,418,000.**
- 2. Chester Bancorp Inc., 1112 State St., Chester IL 62233 (telephone: (618) 826-5038). Holders of Record: 250. Estimated Beneficial Owners: 5,250. Total Assets: \$113,800,000.**
- 3. First Reserve Inc., 1360 South Dixie Highway, Coral Gables FL 33146 (telephone: (305) 667-8871). Holders of Record: 174. Estimated Beneficial Owners: 3,600. Total Assets: \$12,044,409.**
- 4. United Road Services, Inc., 17 Computer Drive West, Albany NY 12205 (telephone: (518) 446-0140). Holders of Record: 294. Estimated Beneficial Owners: 6,100. Total Assets: \$97,767,000.**
- 5. ACAP Corp., 10555 Richmond Ave, 2nd Fl, Houston, TX 77042 (telephone: (713) 974-2242). Holders of Record: 241. Estimated Beneficial Owners: 400. Total Assets: \$146,799,869.**
- 6. Oncure Technologies Corp., Ignacio Valley Road, Suite 300, Walnut Creek, CA 94596 (telephone: (925) 279-2273). Holders of Record: 285. Estimated Beneficial Owners: 6,000. Total Assets: \$32,854,737.**
- 7. SmartDisk Corp., 12780 Westlinks Drive, Fort Myers, FL 33913-8019 (telephone: (239) 425-4000). Holders of Record: 278. Estimated Beneficial owners: 6,000. Total Assets: \$17,172,000.**
- 8. Koala Corp., 7881 S Wheeling Court, Englewood, CO 80112 (telephone: (303) 539-8300). Holders of Record: 114. Estimated Beneficial Owners: 2,300. Total Assets: \$47,076,475.**
- 9. First Federal of Olathe Bancorp, Inc., 100 East Park Street, Olathe, Kansas 66061 (telephone: (913) 782-0026). Holders of Record: 148. Estimated Beneficial Owners: 3,100. Total Assets: \$49,729,000.**
- 10. First Independence Corp., Myrtle & 6th Streets, Independence, KS 67301 (telephone: (316) 331-1660). Holders of Record: 223. Estimated Beneficial Owners: 4,683. Total Assets: \$156,050,000.**
- 11. Lam SW Inc., Unit 25- 32, 2nd Floor, Block B, Focal Ind. C, Man Lok Street, Hunghom, Hong Kong K3 12345 (telephone: (011-852-2766). Holders of Record: 140. Estimated Beneficial Owners: 2,900. Total Assets: \$21,707,000.**

Exhibit B (continued)

12. Webhire Inc., 91 Hartwell Avenue, Lexington, MA 02421 (telephone: (781) 869-5000), Holders of Record: 155. Estimated Beneficial Owners: 3,200. Total Assets: \$12,300,000.

13. Excal Enterprises, Inc., 100 North Tampa Street, Suite 3575, Tampa, FL 33602 (telephone: (813) 224-0228). Holders of Record: 292. Estimated Beneficial Owners: 500. Total Assets: \$16,254,179.

14. Ubics, Inc., 333 Technology Drive, Suite 210, Canonsburg, PA 15317 (telephone: (724) 746-6001). Holders of Record: 69. Estimated Beneficial Owners: 700. Total Assets: \$12,600,000.

15. Guardian International, Inc., 3880 N. 28th Terrace, Hollywood, FL 33020 (telephone: (954) 926-5200). Holders of Record: 157. Estimated Beneficial Owners: 3,200. Total Assets: \$33,900,000.

16. Kimmins Corp., 1501 Second Avenue, East, Tampa, FL 33605 (telephone: (813) 248-3878). Holders of Record: 297. Estimated Beneficial Owners: 1,500. Total Assets: \$77,300,000.

17. Madison Bancshares Group, Ltd., 767 Sentry Parkway West, Blue Bell, PA 19422 (telephone: (215) 641-1111). Holders of Record: 294. Estimated Beneficial Owners: 3,000. Total Assets: \$195,300,000.

18. Isomet Corporation, 5263 Port Royal Road, Springfield, VA 22151 (telephone: (703) 321-8301). Holders of Record: 235. Estimated Beneficial Owners: 2,300. Total Assets: \$9,008,000.

19. Harbourton Financial Corporation, 8180 Greensboro Drive, McLean, VA 22102 (telephone: (703) 883-9757). Holders of Record: 95. Estimated Beneficial Owners: 500. Total Assets: \$31,900,000.

20. Lexington B & L Financial Corp., 205 S. 13th Street, Lexington MO 64067 (telephone: (660) 259-2247). Holders of Record: 281. Estimated Beneficial Owners: 3,000. Total Assets: \$135,900,000.

21. Zachary Bancshares, Inc., 4743 Main Street, Zachary, LA 70791 (telephone: (225) 654-2701). Holders of Record: 266. Estimated Beneficial Owners: 1,000. Total Assets: \$96,700,000.

22. Barrett Business Services, Inc., 4724 SW Macadam Avenue, Portland OR 97239 (telephone: (503) 221-0988). Holders of Record: 162. Estimated Beneficial Owners: 500. Total Assets: \$45,400,000.

23. US Data Corporation, 2435 N. Central Expressway, Richardson, TX 75080 (telephone: (972) 680-9700). Holders of Record: 296. Estimated Beneficial Owners: 2,100. Total Assets: \$8,184,000.

Exhibit B (continued)

24. Neff Corp, 3750 NW 87th Ave, Suite 400, Miami, FL 33178 (telephone: (305) 513-3350). Holders of Record: 97. Estimated Beneficial Owners: 1,000. Total Assets: \$269,757,000.