1666 K Street, N.W.
Washington, DC 20006
Telephone: (202) 207-9100
Facsimile: (202) 862-8433
www.pcaobus.org

Report on

2013 Inspection of Michael T. Studer CPA P.C.
(Headquartered in Freeport, New York)

Issued by the

Public Company Accounting Oversight Board

June 26, 2014

THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT

PORTIONS OF THE COMPLETE REPORT ARE OMITTED FROM THIS DOCUMENT IN ORDER TO COMPLY WITH SECTIONS 104(g)(2) AND 105(b)(5)(A) OF THE SARBANES-OXLEY ACT OF 2002

PCAOB RELEASE NO. 104-2014-157A
(Includes portions of Part II of the full report that were not included in PCAOB Release No. 104-2014-157)

2013 INSPECTION OF MICHAEL T. STUDER CPA P.C.

In 2013, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Michael T. Studer CPA P.C. ("the Firm"). The Board is issuing this report of that inspection in accordance with the requirements of the Sarbanes-Oxley Act of 2002 ("the Act").

The inspection process is designed, and inspections are performed, to provide a basis for assessing the degree of compliance by a firm with applicable requirements related to auditing issuers. The inspection process included reviews of aspects of selected issuer audits completed by the inspected firm. The reviews were intended to identify whether deficiencies existed in those aspects of the audits, and whether such deficiencies indicated weaknesses or defects in the firm's system of quality control over audits. In addition, the inspection included review of policies and procedures related to certain quality control processes of the firm that could be expected to affect audit quality.

The issuer audits and aspects of those audits inspected were selected based on a number of risk-related and other factors. Due to the selection process, the deficiencies included in this report are not necessarily representative of the Firm's issuer audit practice.

The Board is making portions of the report publicly available. Specifically, the Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report.[1]

[1] In its *Statement Concerning the Issuance of Inspection Reports*, PCAOB Release No. 104-2004-001 (August 26, 2004), the Board described its approach to making inspection-related information publicly available consistent with legal restrictions. As described there, if the nonpublic portions of any inspection report discuss criticisms of or potential defects in a firm's system of quality control, those discussions also could eventually be made public, but only to the extent a firm fails to address the criticisms to the Board's satisfaction within 12 months of the issuance of the report.

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's inspection staff ("the inspection team") conducted primary procedures for the inspection from June 24, 2013 to June 28, 2013. These procedures were tailored to the nature of the Firm, certain aspects of which the inspection team understood at the outset of the inspection to be as follows:

Number of offices	1 (Freeport, New York)
Ownership structure	Professional corporation
Number of partners	1
Number of professional staff[2]	6
Number of issuer audit clients[3]	31

[2] "Professional staff" includes all personnel of the Firm, except partners or shareholders and administrative support personnel. The number of partners and professional staff is provided here as an indication of the size of the Firm, and does not necessarily represent the number of the Firm's professionals who participate in audits of issuers or are "associated persons" (as defined in the Act) of the Firm.

[3] The number of issuer audit clients shown here is based on the Firm's self-reporting and the inspection team's review of certain information for inspection planning purposes. It does not reflect any Board determination concerning which, or how many, of the Firm's audit clients are "issuers" as defined in the Act. For information about audit reports issued by the Firm, see Item 4.1 of the Firm's annual reports on PCAOB Form 2, available at www.pcaobus.org.

A. Review of Audit Engagements

The inspection procedures included a review of aspects of the Firm's auditing of financial statements of four issuers. The inspection team identified what it considered to be audit deficiencies. The deficiencies identified in three of the audits reviewed included deficiencies of such significance that it appeared to the inspection team that the Firm, at the time it issued its audit report, had not obtained sufficient appropriate audit evidence to support its opinion on the issuer's financial statements or internal control over financial reporting ("ICFR"). Those deficiencies were –

Issuer A

(1) the failure, in an audit of ICFR, to perform procedures to test the operating effectiveness of controls;

(2) the failure to perform sufficient procedures to test the occurrence, completeness, and valuation of revenue;

(3) the failure to perform sufficient procedures to test the existence and valuation of inventory, including the use of sampling with an inadequate sample size developed without consideration of appropriate factors;

Issuer B

(1) the failure to perform sufficient procedures to test the occurrence, completeness, and valuation of revenue, including the use of sampling with an inadequate sample size developed without consideration of appropriate factors;

(2) the failure to perform sufficient procedures to test the existence of accounts receivable;

(3) the failure to perform sufficient procedures to evaluate intangible assets for impairment; and

Issuer C

(1) the failure to perform sufficient procedures to test the allowance for doubtful accounts.

One of the deficiencies described above related to auditing an aspect of an issuer's financial statements that the issuer revised in a restatement subsequent to the primary inspection procedures.[4]

B. Auditing Standards

Each of the deficiencies described in Part I.A of this report represents circumstances in which it appeared to the inspection team that the Firm failed to comply with the requirement to obtain sufficient appropriate audit evidence to support its opinion that the financial statements were presented fairly, in all material respects, in accordance with applicable accounting principles, and for its opinion concerning whether the issuer maintained, in all material respects, effective ICFR. Each deficiency relates to several applicable standards that govern the conduct of audits.

AU 230, *Due Professional Care in the Performance of Work* ("AU 230"), requires the independent auditor to plan and perform his or her work with due professional care. AU 230 and PCAOB Auditing Standard No. 13, *The Auditor's Responses to the Risks of Material Misstatement* ("AS No. 13"), specify that due professional care requires the exercise of professional skepticism. This is an attitude that includes a questioning mind and a critical assessment of the appropriateness and sufficiency of audit evidence.

AS No. 13 requires the auditor to design and implement audit responses that address the identified risks of material misstatement, and PCAOB Auditing Standard No. 15, *Audit Evidence* ("AS No. 15"), requires the auditor to plan and perform audit procedures to obtain sufficient appropriate audit evidence to provide a reasonable basis for the audit opinion. Sufficiency is the measure of the quantity of audit evidence, and the quantity needed is affected by the risk of material misstatement and the quality of the audit evidence obtained. The appropriateness of evidence is measured by its

[4] The Board inspection process did not include review of any additional audit work related to the restatement.

quality; to be appropriate, evidence must be both relevant and reliable in support of the related conclusions.

PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* ("AS No. 5"), and AS No. 13 establish requirements regarding testing and evaluating ICFR. In an audit of ICFR in an integrated audit, AS No. 5 requires the auditor to plan and perform the audit to obtain appropriate evidence that is sufficient to support the auditor's opinion on ICFR as of the date of that opinion. AS No. 13 requires that, if the auditor plans to assess control risk at less than the maximum and to base the nature, timing, and extent of substantive procedures on that lower assessment, the auditor must obtain evidence that the controls tested were designed and operating effectively during the entire period for which the auditor plans to rely on controls to modify the substantive procedures.

Each deficiency described in Part I.A of this report involves, in the inspection team's view, a failure to comply with the provisions cited above and also a failure to perform, or perform sufficiently, certain specific audit procedures that are required by other applicable auditing standards. The table below lists the other specific auditing standards that are primarily implicated by the deficiencies identified in Part I.A of this report.[5]

PCAOB Auditing Standards	Issuers
AU 330, *The Confirmation Process*	B
AU 342, *Auditing Accounting Estimates*	B, C
AU 350, *Audit Sampling*	A, B

[5] This table does not necessarily include reference to every auditing standard that may have been implicated by the deficiencies included in Part I.A.

C. Review of Quality Control System

In addition to evaluating the quality of the audit work performed on specific audits, the inspection included review of certain of the Firm's practices, policies, and procedures related to audit quality. This review addressed practices, policies, and procedures concerning audit performance, training, compliance with independence standards, client acceptance and retention, and the establishment of policies and procedures. Any defects in, or criticisms of, the Firm's quality control system are discussed in the nonpublic portion of this report and will remain nonpublic unless the Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

D. General Information Concerning PCAOB Inspections

Board inspections are designed to identify whether weaknesses and deficiencies exist related to how a firm conducts audits and addresses any such weaknesses and deficiencies. To achieve that goal, Board inspections include reviews of certain aspects of selected audits performed by the firm and reviews of other matters related to the firm's quality control system. The scope of the inspection procedures is determined according to the Board's criteria, and the firm is not allowed an opportunity to limit or influence the scope. The focus on weaknesses and deficiencies necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools. Further, the inclusion in an inspection report of certain deficiencies and potential deficiencies should not be construed as an indication that the Board has made any determination about other aspects of the firm's systems, policies, procedures, practices, or conduct not included within the report.

In the course of reviewing aspects of selected audits, an inspection may identify ways in which a particular audit is deficient, including failures by the firm to identify, or to address appropriately, respects in which an issuer's financial statements do not present fairly the financial position, results of operations, or cash flows of the issuer in conformity with Generally Accepted Accounting Principles ("GAAP").[6] It is not the

---

[6] When it comes to the Board's attention that an issuer's financial statements appear not to present fairly, in a material respect, the financial position, results of operations, or cash flows of the issuer in conformity with applicable accounting principles, the Board's practice is to report that information to the Securities

purpose of an inspection, however, to review all of a firm's audits or to identify every respect in which a reviewed audit is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audits, or its issuer clients' financial statements or reporting on internal control, are free of any deficiencies not specifically described in an inspection report.

In some cases, an inspection team's observation that a firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if a firm claims to have performed the procedure. PCAOB Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"), provides that, in various circumstances including PCAOB inspections, a firm that has not adequately documented that it performed a procedure, obtained evidence, or reached an appropriate conclusion must demonstrate with persuasive other evidence that it did so, and that oral assertions and explanations alone do not constitute persuasive other evidence. See AS No. 3, paragraph 9 and Appendix A to AS No. 3, paragraph A28. For purposes of the inspection, an observation that the Firm did not perform a procedure, obtain evidence, or reach an appropriate conclusion may be based on the absence of such documentation and the absence of persuasive other evidence.

Inclusion of a deficiency in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. Under PCAOB standards, when audit deficiencies are discovered after the date of the audit report, a firm must take appropriate action to assess the importance of the deficiencies to the firm's present ability to support its previously expressed audit opinions.[7] Depending upon the circumstances, compliance with these standards may require the firm to perform additional procedures, or to inform a client of the need for changes to its

---

and Exchange Commission ("SEC" or "Commission"), which has jurisdiction to determine proper accounting in issuers' financial statements. Any description in this report of financial statement misstatements or failures to comply with SEC disclosure requirements should not be understood as an indication that the SEC has considered or made any determination regarding these issues unless otherwise expressly stated.

[7] See AU 390, *Consideration of Omitted Procedures After the Report Date* ("AU 390"), and AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report* ("AU 561") (both included among the PCAOB's interim auditing standards, pursuant to PCAOB Rule 3200T), and AS No. 5 paragraph 98.

financial statements or reporting on internal control, or to take steps to prevent reliance on previously expressed audit opinions. A Board inspection does not typically include review of a firm's actions to address deficiencies identified in that inspection, but the Board expects that firms are attempting to take appropriate action, and firms frequently represent that they have taken, are taking, or will take, action. If, through subsequent inspections or other processes, the Board determines that the firm failed to take appropriate action, that failure may be grounds for a Board disciplinary sanction.

END OF PART I

PORTIONS OF THE REST OF THIS REPORT ARE NONPUBLIC AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

PART II

* * * *

B. Issues Related to Quality Controls

The inspection of the Firm included consideration of aspects of the Firm's system of quality control.[8] QC 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice* ("QC 20"), provides that an auditing firm has a responsibility to ensure that its personnel comply with the applicable professional standards. This standard specifies that a firm's system of quality control should encompass the following elements: (1) independence, integrity, and objectivity; (2) personnel management; (3) acceptance and continuance of clients and engagements; (4) engagement performance; and (5) monitoring.

Assessment of a firm's quality control system rests both on review of a firm's stated quality control policies and procedures and on inferences that can be drawn from identified deficiencies in audit performance. These deficiencies, whether alone or when aggregated, may indicate areas where a firm's system has failed to provide reasonable assurance of quality in the performance of audits. Even deficiencies that do not result in an insufficiently supported audit opinion may indicate a defect in a firm's quality control system.[9] Defects in a firm's quality control system may also be identified through inspection procedures that are specifically focused on aspects of the firm's system of quality control.

[8] This report's description of quality control issues is based on the inspection team's observations during the primary inspection procedures. Any changes or improvements that the Firm may have made in its system of quality control since that time may not be reflected in this report, but will be taken into account by the Board during the 12-month remediation process following the issuance of this report.

[9] Not every audit deficiency suggests a possible defect in a firm's quality control system, and this report does not discuss every audit deficiency the inspection team identified.

Audit Performance

A firm's system of quality control should provide reasonable assurance that the work performed on an audit engagement will meet applicable professional standards and regulatory requirements. On the basis of the information reported by the inspection team, including the audit performance deficiencies described in Part II.A (and summarized in Part I.A) and any other deficiencies identified below, the Board has concerns that the Firm's system of quality control fails to provide such reasonable assurance in at least the following respects –

Testing Appropriate to the Audit

The Firm's system of quality control appears not to provide sufficient assurance that the Firm will conduct all testing appropriate to a particular audit, specifically with respect to the following issues:

* * * *

Allowance for Doubtful Accounts

As discussed above, in one the audits reviewed, the inspection team identified a significant deficiency related to the Firm's testing of the allowance for doubtful accounts. This information provides cause for concern regarding the Firm's quality control policies and procedures related to the auditing of the allowance for doubtful accounts. [Issuer C]

Fraud Procedures

The Firm's system of quality control appears not to provide sufficient assurance that the Firm will perform all of the required procedures in accordance with the provisions of PCAOB Auditing Standard No. 12, *Identifying and Assessing Risks of Material Misstatement*; AS No. 13; and AU 316, *Consideration of Fraud in a Financial Statement Audit.* Specifically, the Firm (1) did not perform procedures to test journal entries and other adjustments for evidence of possible material misstatements due to fraud [Issuers A and B]; (2) did not perform procedures to identify and assess fraud risk factors [Issuers A and B]; (3) did not apply appropriate analytical procedures [Issuers A and B]; (4) did not perform procedures to support its conclusion that the presumption of revenue as a fraud risk was overcome [Issuers A and B]; (5) did not perform unpredictable procedures [Issuers A and B]; (6) did not hold a brainstorming discussion among engagement personnel regarding the risk of material misstatement due to fraud [Issuer B]; and (7) did not make inquiries of the audit committee, or equivalent, management and others within the entity to obtain their views about the risks of fraud and how they are addressed [Issuer B].

Engagement Quality Review

In light of the audit performance deficiencies described in Part II.A (and summarized in Part I.A), questions exist about the effectiveness of the Firm's system of quality control with respect to the execution of engagement quality reviews in compliance with PCAOB Auditing Standard No. 7, *Engagement Quality Review* ("AS No. 7"). An engagement quality review performed with due care in compliance with AS No. 7 should have detected, and resulted in the Firm addressing, each of the deficiencies described in Part II.A. [Issuers A, B, and C]

* * * *

Monitoring and Addressing Identified Weaknesses

The Firm's system of quality control appears to lack a monitoring element sufficient to provide the Firm with reasonable assurance that the Firm's policies and procedures are suitably designed and effectively applied in accordance with QC 20. The Firm's monitoring appears to have been deficient with respect to at least two types of previously identified weaknesses. An inspection of the Firm conducted in 2010 identified to the Firm that the Firm had failed in certain of its audits to perform sufficient procedures related to the allowance for doubtful accounts and certain fraud procedures, including testing journal entries and other adjustments for evidence of possible material misstatements due to fraud and applying appropriate analytical procedures. An appropriate approach to monitoring would have resulted in the Firm avoiding these deficiencies in audits performed after they were brought to the Firm's attention, yet similar deficiencies were noted in this inspection.

* * * *

PART IV

RESPONSE OF THE FIRM TO DRAFT INSPECTION REPORT

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Firm provided a written response to a draft of this report. Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report.[10]

[10] The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In some cases, the result may be that none of a firm's response is made publicly available. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits from, or any inaccurate statement in the draft that the Board corrects in, the final report.

MICHAEL T. STUDER CPA P.C.
18 East Sunrise Highway, Suite 311
Freeport, NY 11520
Phone: (516) 378-1000
Fax: (516) 546-6220

April 30, 2014

Ms. Helen A. Munter, Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006

Re: Response to Part IA (Review of Audit Engagements) of the Draft Report of Inspection dated March 31, 2014

Dear Ms. Munter:

This letter responds to comments contained in Part IA (Review of Audit Engagements) of the Draft Report of Inspection dated March 31, 2014.

For your convenience, we have included each of the comments in italics before each of the Firm's responses.

Issuer A

(1) *The failure, in an audit of ICFR, to perform procedures to test the operating effectiveness of controls;*

Response:

We understand the PCAOB's concern that the Firm failed to perform procedures to test the operating effectiveness of controls, as of December 31, 2011.

As we documented in the Exhibit A received by the PCAOB Inspection Team on June 24, 2013, this Issuer received a routine SEC Inquiry Letter concerning the year ended December 31, 2011 10K on May 7, 2012. In follow-up correspondence between the SEC and the Company, one issue that came up related to whether the Company qualified as a smaller reporting company under Item 10(f) of Regulation S-K, or should continue to file as an accelerated filer subject to, among other things, ICFR compliance under Sarbanes-Oxley. While in a letter to the Company on July 3, 2013 the SEC indicated that the Company did not meet the requirements to be qualified as a smaller reporting company under Item 10(f) of Regulation S-K, the level of internal controls over financial reporting suitable to this Issuer, and auditor testing thereof, should consider a number of financial metrics for this Issuer. These include:

1) Annual sales volume for the year ended December 31, 2011 is $286,000, or approximately $24,000 per month. The level of the sales volume from year to year is relatively stable, even though in a declining trend. The Firm believes the risk of misstatement due to a failure in controls related to accounts receivable/sales is primarily addressed by substantive tests performed in the financial statements audit.

2) Payroll costs are included in the determination of inventory and cost of sales and administrative expenses within operating expenses. Payroll costs, which are relatively stable with moderate year to year increases, amounted to approximately $278,000 in the year ended December 31, 2011. Payroll costs represent a minimum number of personnel, most of which are involved in manufacturing and delivery of products from BCRA's Saint Gonnery France facility. The Firm believes the risk of misstatement due to a failure in controls related to payroll is primarily addressed by substantive tests performed in the financial statements audit.

3) Operating expenses for the year ended December 31, 2011 of $681,000 included depreciation and amortization of $94,000, consulting and professional fees of $213,000 and payroll of $139,000. Depreciation and amortization and related patent cost acquisitions are computed and vouched, respectively; with impairment considerations also evaluated by substantive tests performed in the financial statements audit. In addition, consulting and professional fees are also routinely analyzed in the financial statements audit. Consequently the amount of operating expenses that might be subject to misstatement due to poor ICFR controls is limited.

4) Based on the Company's annual sales volume, the Company's cost of sales, after removing payroll of $139,000, is approximately $71,000 for the year ended December 31, 2011. Consequently the amount of cost of sales that might be subject to misstatement due to poor ICFR controls is limited.

5) Accounts payable at December 31, 2011 of $649,000 include $388,000 to Issuer A's patent service company. The Firm believes that substantive procedures performed related to the accounts payable at December 31, 2011 sufficiently address payables recorded at that date and controls related to accounts payable. Consequently, amounts in accounts payable that might be subject to misstatement due to poor ICFR controls is limited.

Essentially, the Firm believes, given 1) - 5) above, and the fact that substantive procedures are applied during the audit to debt, accrued interest payable and interest expense, the principal risk of misstatement due to fraud relates to the existence and valuation of inventory, for which meaningful substantive tests may better address that risk in this Issuer situation than tests of controls.

Testing of Operating Effectiveness

Issuer A has a minimum number of personnel, most of which are involved in manufacturing and delivery of products from its Saint Gonnery France facility. Internal control over financial reporting ("ICFR") is performed primarily by Issuer A's CEO, and two accounting firms (one French firm for Issuer A's French operating subsidiary; one U.S. PCAOB Registered Firm for Issuer A and all other subsidiaries other than the French subsidiary) engaged by Issuer A. Due to cost/benefit considerations, the CEO is often in the position that he is responsible both for the performance of a specific accounting or control function and testing and documenting his own performance. Although not necessarily documented in our work papers, we determined, through both performing our financial statements audit and through "walk-throughs" of transactions in the basic cycles (cash receipts disbursements, accounts receivable/sales, inventory/purchases and payroll), that identified important controls were operating as designed in all material respects and that persons performing the controls possessed the necessary authority and competence to perform the control effectively.

Evaluation of Effect of Substantive Auditing Procedures on ICFR

The significant misstatements noted in the audit of the financial statements related to inventory costing. However, the misstatements noted were the result of the same error (i.e., the issuer's failure to update components of the standard cost from French Francs to Euros for certain products manufactured prior to 2002) and management was able to successfully isolate and correct those errors. Although not necessarily documented in our work papers, we concluded that the effect of the findings of the substantive auditing procedures performed in the audit of the financial statements should not result in an opinion that Issuer A's ICFR was not effective.

(2) *The failure to perform sufficient procedures to test the occurrence, completeness, and valuation of revenue;*

Response:

The Firm's work papers reflect the testing of 10 sales invoices ($18,054) reflected within sales for the year ended December 31, 2011 per the sales cutoff it performed at December 31, 2011. In our review of Firm work papers for our audit at December 31, 2010, we determined that 5 sales invoices ($2,477) for sales during the year ended December 31, 2011 were tested in the sales cutoff during the prior year's audit. So, the Firm tested $20,531 out of the sales of $$286,548 for the year ended December 31, 2011, or 7%. At the suggestion of the PCAOB Team, the Firm prepared a PCA-CX-8.1 and a PCA-CX-8.2 for the purpose of determining the number of items that might be appropriate for a more random test of sales transactions throughout the year. The sample suggested 19 items be tested (at line 11 on PCAP-CX-8.2), none of which sample items were individually significant sales invoices. The actual sample size used by the Firm was 15 items (CX-8.2, page 4, <A>).Based on that, the Firm has concluded that utilizing the PCA-CX-8.1- Planning Worksheet to Determine Extent of Substantive Procedures and 8.2 – Sample Planning and Evaluation Form – Substantive Procedures driven sample in future audits of sales is likely to produce a workable and random sampling of sales transactions during an audit of Company sales for the year under audit.

(3) *The failure to perform sufficient procedures to test the existence and valuation of inventory, including the use of sampling with an inadequate sample size developed without consideration of appropriate factors;*

Response:

1. The Issuer's initial misstatements identified in the items subject to standard cost testing were the result of the same error (i.e., the Issuer's failure to update components of the standard cost from French Francs to Euros for certain products manufactured prior to 2002). The Firm identified the cost error in its initial sampling of 13 individual inventory items (originally totaling 89,953 Euros - $116,480) for the purpose of testing inventory pricing (cost) and lower of cost or market, when that initial test identified inventory items in the lower of cost or market test at a cost in excess of market.

   After the Firm encountered the French Franc to Euro inventory pricing problem in its test of the 13 items (89,953 Euros originally as priced became 37,637 Euros - $ 48,736), it advised the Issuer of the misstatements. The Issuer and Consultaudit (the French auditor of the Issuer's French subsidiary) reviewed the remainder of the inventory items for similarly mispriced inventory and provided the Firm a corrected inventory. The Firm then selected an additional 9 finished goods items for testing (20,408 Euros - $26,426) and no cost errors were noted. Accordingly, as indicated in the evaluation of the test results in the PCA-CX-8.2 in Exhibit 1, the $67,744 error was not projected to the remaining finished goods and work in process inventory population of $382,761.

   It is important to note that the Firm was the principal auditor of the Issuer for the year ended December 31, 2011 and performed an audit of the French subsidiary, principally using ConsultAudit solely for the observation of the inventory in France, and utilizing analyses and financial statements prepared by ConsultAudit that the Firm used in performing the audit of the French subsidiary.

2. The Issuer has a history of resterilization of older inventory items and inclusion in the sales catalog of only non obsolete products. The Issuer also has a very small number of administrative personnel. In the limited time that the Firm's audit person arrived in France, and after his return to the United States, it is difficult for the Issuer to locate sales invoices subsequent to the balance sheet date, as well as invoices for sales during the year then ended. The Firm's experience auditing this particular Issuer suggests, and the Firm believes, that due to the Issuer's practice of routinely resterilzing product for sale that listing of a product in the sales catalog is good evidence that a product is being sold, similar to that of examining an invoice.

   During the year ended December 31, 2011, the Firm's work papers contain inventory agings by year for the year ended December 31, 2011 and for the year ended December 31, 2010 prepared by the Firm's audit staff for the purpose of reviewing reductions in inventory representing sales of product older than one year from date produced to determine whether older inventory aging categories continued to have current sales. The Firm proposed an adjusting entry (which the Issuer recorded) to increase the reserve for slower moving finished goods inventories by $46,339 from $75,720 to $122,059. Exhibit 3 is an email dated April 19, 2012 and attachment that includes comparative inventory agings at December 31, 2011 and December 31, 2010 that demonstrate projected inventory reductions made by the Firm related to older product expected to be sold subsequent to December 31, 2011 (in 2012). This Firm prepared a pdf schedule, which was inadvertently not included in work papers provided to the PCAOB Inspection Team, demonstrating that a thorough evaluation of reserves needed for slower moving inventory was performed by the Firm. The Firm also believes it also demonstrates that an item listed in the catalog (because it still sells beyond one year from the date it was produced because of the Company's routine re-sterilizaton process) is a satisfactory substitute for a sales invoice examination in performing a lower of cost or market test on individual inventory items.

3. The raw materials inventory of $69,581 at December 31, 2011 consisted of coral ($32,796 gross, $27,359 net) and packaging articles ($36,785 gross, $22,330 net) largely purchased in years prior to 2011 and subject to cost testing in prior year audits. Additions in 2011 were insignificant. Raw material inventory was $77,457 at December 31, 2010. Accordingly, raw materials inventory decreased by $7,876 from December 31, 2010 to December 31, 2011 (or 10%), while sales revenue for the same period decreased by 7% (2010 sales of $307,655 less 2011 sales of $286,548 = $21,107 decrease; $21,107 decrease divided by 2010 sales of $307,655 = 7%). The Firm believes it is highly unlikely that raw materials inventory, which represents a relatively small and stable component of the total inventories, would have any significant price testing discrepancies that would warrant expanded tests as suggested by that component representing 12% of inventory.

4. Based on the relatively small and stable component that raw materials represents out of total inventories described in 3. above, the Firm believes reviewing test count discrepancies with management were sufficient procedures in the circumstances.

Issuer B

(1) *The failure to perform sufficient procedures to test the occurrence, completeness, and valuation of revenue, including the use of sampling with an inadequate sample size developed without consideration of appropriate factors;*

(2) *The failure to perform sufficient procedures to test the existence of accounts receivable;*

Response:

Shipping Documents

The Firm understands the importance of performing sufficient procedures to test the existence, completeness, and valuation of revenue in accordance with Auditing Standard No. 15, Audit Evidence, ("AS 15"). In particular, the Firm understands the PCAOB Inspection Team's assertion that by not reviewing shipping documents, the Firm failed to perform procedures to demonstrate that revenue was recognized in the proper period.

Shipping documentation as related to accounts receivable at March 31, 2012 is discussed under "Alternate Procedures on 13 Non-responding Accounts Receivable Confirmations" below.

In order for the Firm to refresh on the status of remainder accounts receivable at March 31, 2012 for Customer 1 of $29,300 and Customer 2 of $21,658, and revenue recognized under each contract during the year then ended, the Firm currently prepared a rollforward of activity for both customers, utilizing information from e-mails that follow the 2 rollforwards in Exhibit 1 on pages 2/29 and 3/29. The rollforward of Customer 1 corroborates that the Firm had determined that the Company had recognized revenue on Customer 1 on an invoicing in the quarter ended December 31, 2011 for which $53,377 was recognized by the Company in the year ended March 31, 2012 and that an on account payment of $24,077 was not included in deferred revenue at March 31, 2012, while the reserve for doubtful accounts at that date had a provision of $21,975 in financial statements issued. The information also corroborates that the Firm had determined in the prior year's audit that pursuant to a contract the Issuer had recognized $101,040 from delivery and acceptance of the amounts due under the Customer 1 contract during the year ended March 31, 2011.

Similarly, as described in the preceding paragraph, the Firm determined that the $21,658 in accounts receivable at March 31, 2012 for Customer 2 arose from revenue recognized under a contract for which the Company initially recognized revenue of $86,070 in the year ended March 31, 2011, but reversed revenue of $32,851 in the final financial statements issued for the year then ended. Consequently, the Company recognized revenue from an invoice it rendered in the quarter ended June 30, 2011 under that contract of $32,851. Since the Company only collected $9,591 in the quarter ended June 30, 2011, upon further reflection by the Freeport Audit Team it appears that the Company has chosen to absorb the remainder of $23,260, in the hopes of obtaining future business from Customer 2 – rather than being unable to collect from that customer.

The Firm also refreshed on the status of Customer 3 from which the Company recognized revenue of $135,000 during the year ended March 31, 2012, of which it collected $103,000 during the year then ended. Upon the Firm's current/remedial review, the Issuer absorbed $32,000 during the year ended March 31, 2012 against that $135,000, in the hope of obtaining future business from the customer that is apparently not a doubtful account. In an e-mail dated February 11, 2012, the Firm received the first of 4 installments containing the contract dated June 30, 2011 from the Issuer's CEO for this customer. On page 12/13 in support of the PCA-CX-8.2 described under "Sample Size for Testing Revenue" below, the contract that supports the revenue to be recognized by the Issuer was examined by the Firm's Freeport Audit Staff person performing this year end audit.

The Firm has reflected on the PCA-CX-8.2 support in Exhibit 3 on page 12/13. Based on reflection, it believes that work at the interim reviews is sufficient evidence that Customer 3's revenue recognized of $103,000 during the year ended March 31, 2012 constitutes the Firm testing shipping for that item. The Firm believes that the work performed related to Customer 4 that resulted in a revenue reversal constitutes testing of shipping during the year ended March

31, 2012 in that amount. As described under "Alternate Procedures on 13 Non-responding Accounts Receivable Confirmations" below:

> The Firm also recognized that based on resolution of the revenue recognition issues related to the year ended March 31, 2012, Issuer B should also be advised that the Firm needs to review similar information concerning amounts recorded related to revenue recognition in the interim reviews for the quarters ended June 30, 2011, September 30, 2011 and December 31, 2011 10Q's in the year ended March 31, 2012; and the quarter ended June 30, 2012 10Q.

Accordingly, the Firm understands and agrees that it needs to do a better job in situations like this on this and other issuers to test delivery and customer acceptance throughout the year, to preclude incidences of premature revenue recognition that may have a significant impact on year end and interim results.

Sample Size for Testing Revenue

As suggested by the PCAOB Inspection Team, we currently prepared PPC forms CX-8.1 and CX-8.2 and sent them to the Inspection Team on 7/1/13. CX-8.2 page 2 suggests a sample size of 104. It is likely better documented interim testing brought forward to the audit work papers that involves significant contracts might produce individually significant items tested via the review of contracts. In addition, that interim review work brought forward might better substantiate ongoing sales testing for delivery and customer acceptance that might reduce a suggested sample in the PCA-CX-8.1, so that the suggested testing of more than 100 items might not be necessary at year end. Since a restatement of quarterly results was found to be likely, more revenue testing has been done by the Firm, as a byproduct of subsequent due diligence work related to the potential restatement of the quarters. Accordingly, the Firm agrees that in future testing of revenue that the sample size should be larger and more representative of the population being tested.

Alternate Procedures on 13 Non-responding Accounts Receivable Confirmations

Based on the PCAOB Inspection Team's Comment concerning the Firm's possible failure to perform alternate procedures on the 14 non-responding accounts receivable confirmations, the Firm has remedially (currently) prepared a Confirmation Reconciliation Excel for the Accounts Receivable that were outstanding at March 31, 2012, utilizing information available in work papers of the Firm when the audit was performed, some of which work papers were inadvertently not provided to the Inspection Team in the package given to them on their arrival on June 24, 2013; or provided to them in the course of their short field inspection. In our discussions in this section, any such work papers provided to the Inspection Team were submitted with relevant e-mail that date stamps when this material was available and used by the Firm's Freeport Audit Staff person. In preparing these Confirmation Reconciliations for the 2 entities whose accounts receivable made up the balance at March 31, 2012 in financial statements issued for Issuer B, the Firm recognizes that it was deficient in not routinely preparing this type of reconciliation to better account for accounts receivable for which no responses had been received from the customer by performing more suitable alternative procedures concerning amounts that were indicated as unverified. The Firm believes it was remiss in not preparing these reconciliations, and understands that it must routinely prepare them in similar circumstances on the Issuer and others.

The Confirmation Reconciliation Excel includes both of the Issuer's operating subsidiaries. We noted that Accounts Receivable confirms cycled for requested reply by customers for one subsidiary totaled $125,119. However, of the 10 customers selected, all were invoiced in the 4th quarter of the year ended March 31, 2012, and all had on account payments received from the customer that totaled $132,831, each of which represented approximately a 50% downpayment. Accordingly, for this subsidiary before the on account deposit, the gross balance was $257,950. While the Company reversed revenue of $34,000 and provided a 50% reserve for doubtful accounts of $50,000, in preparing this entity's Confirmation Reconciliation, the Firm now questions whether its procedures concerning the accounts receivable were sufficiently vigorous on this entity to ascertain whether delivery and acceptance by the customer in fact took place by March 31, 2012, since subsequent collections aggregated $8,545 for this entity's customers, of which $7,145 related to those cycled for confirmation.

In properly preparing these reconciliations, we noted that Accounts Receivable confirms cycled for requested reply by customers for the other subsidiary totaled $236,794 for 4 customers selected, of which 3 were invoiced in the 4th quarter of the year ended March 31, 2012 that totaled $215,136. However, for this subsidiary the Company reversed revenue of $197,920 for one customer (Customer 4) that it had initially recognized as earned in the year ended March 31, 2012 and provided a 75% reserve for doubtful accounts of $39,662. That $39,662 reserve included $16,243 related to a receivable for Customer 2 that arose in the quarter ended June 30, 2011 for which the reserve related to an unverified /unconfirmed receivable on this entity of $21,658. Another $21,975 of the reserve at March 31, 2012 related to Customer 1. In preparing this entity's Confirmation Reconciliation, the Firm now questions whether its procedures concerning the accounts receivable were sufficiently vigorous on this entity to ascertain whether delivery and acceptance by the customer in fact took place by March 31, 2012, since subsequent collections aggregated $211,068 for this entity's customers, of which $199,620 related to those cycled for confirmation (including $197,920 for Customer 4 whose receivable/revenue recognized was reversed in the year ended March 31, 2012). However, in reviewing information available in certain work papers not provided the PCAOB Inspection Team, the Firm Freeport Audit staff determined that contracts and other information was examined by the Firm for Customer 2 and Customer 1.

In the Firm assessing whether it failed to perform alternate procedures on the 14 non-responding accounts receivable confirmations, the Firm reacquainted itself with the Company's policy for recognizing revenue, which was summarized in an e-mail dated June 25, 2011 received by the Freeport Audit Staff person assigned to this engagement from the President of the Company, which stated:

> A customer shows interest in our product, either through a show or via advertising. Thereafter he is given a demo. Once he decides which products he is interested in, an invoice is created and sent to the customer. The sale is only considered a sale once the

funds have been credited to the account and booked. Once the funds of the purchaser have hit the account, our engineers are advised that they can deliver and proceed. The Polish engineers are notified on a daily basis what monies have hit the account and from which source.

The transaction is recorded on our financial system and booked.

With a few exceptions (i.e., some large contracts involving both products and services and some sales under installment payment arrangements introduced in year ended 3/31/12), enabling or electronic delivery of the issuer's products is made simultaneously with the receipt of the sales price in cash from the respective customer. No physical delivery of products is required. Accordingly, where deemed necessary, the Firm reviewed contracts containing delivery terms and other available delivery documentation.

In order for the Firm to refresh on the status of remainder accounts receivable at March 31, 2012 for Customer 1 of $29,300 and Customer 2 of $21,658, and revenue recognized under each contract during the year then ended, the Firm currently prepared a rollforward of activity for both customers. The rollforward of Customer 1 corroborates that the Firm had determined that the Company had recognized revenue on Customer 1 on an invoicing in the quarter ended December 31, 2011 for which $53,377 was recognized by the Firm in the year ended March 31, 2012 and that an on account payment of $24,077 was not included in deferred revenue at March 31, 2012, while the reserve for doubtful accounts at that date had a provision of $21,975 in financial statements issued. The information also corroborates that the Firm had determined in the prior year's audit that pursuant to a contract the Issuer had recognized $101,040 from delivery and acceptance of the amounts due under the Customer 1 contract during the year ended March 31, 2011.

Similarly, as described in the preceding paragraph, the Firm determined that the $21,658 in accounts receivable at March 31, 2012 for Customer 2 arose from revenue recognized under a contract for which the Company initially recognized revenue of $86,070 in the year ended March 31, 2011, but reversed revenue of $32,851 in the final financial statements issued for the year then ended. Consequently, the Company recognized revenue from an invoice it rendered in the quarter ended June 30, 2011 under that contract of $32,851. Since the Company only collected $9,591 in the quarter ended June 30, 2011, upon further reflection by the Freeport Audit team, it appears that the Company has chosen to absorb the remainder of $23,860, in the hopes of obtaining future business from Customer 2 – rather than being unable to collect from that customer.

We prepared a summary proposed adjustment, as an attachment to our response to the Inspection Team's Comment Form, that would be necessary should the Company be unable to support delivery and acceptance by the customer related to accounts receivable outstanding at March 31, 2012 based on the information assembled in preparing the Confirmation Reconciliation Excels for the 2 entities.

We also prepared, as an attachment to the Comment Form, a similar Confirmation Reconciliation for the 2 entities at March 31, 2011, for the purpose of the Firm considering what effect, if any, such procedure would suggest was the impact of possible revenue reversal in the year ended March 31, 2011 on the reported results as filed by the Company for the year ended March 31, 2012.

We also prepared currently/remedially prepared analysis showing the adjusted results for the year ended March 31, 2012, pending the Firm's obtaining better proof that delivery and customer acceptance took place prior to March 31, 2012, that the Firm recognized would be necessary from the Issuer, and if not provided would require consideration by the Issuer of a restatement of its financial statements for the year ended March 31, 2012. If such information could not be timely provided, the Issuer was advised by the Firm that an 8K nonreliance needed to be timely filed for the March 31, 2012 10K until the matter is resolved.

The preliminary adjustment described in the preceding paragraph would be necessary in the Firm's opinion because:

Revenues as revised would be $4,184,593 for the year ended March 31, 2012, a decrease of $369,529 from that originally reported of $4,554,122, or 8.1%. However, instead of a trend in increasing of revenue from 2011 to 2012 of 3.6%, there would be a decline of 4.8%.

Gross profit as revised would be $1,552,396 for the year ended March 31, 2012, a decrease of $369,529 from that originally reported of $1,921,925, or 19.2%. In addition, the revised Gross profit rate would be 37% for the year ended March 31, 2012, versus the originally reported Gross profit rate of 42%.

The Loss from operations as revised would be $1,461,124 for the year ended March 31, 2012, an increase of $279,867 from that originally reported of $1,181,257, or 23.7%.

Accounts receivable reported in Assets as revised would be $-0- at March 31, 2012, a decrease of $106,691 from that originally reported of $106,691 or 100.0%. Total current assets would also be decreased by 23.7% from $450,179 to $343,488 at March 31, 2012.

Deferred revenue reported in Liabilities as revised would be $354,679 at March 31, 2012, an increase of $173,176 from that originally reported of $181,503, or 95.4%. Total current liabilities would also be increased by 26.6% from $650,346 to $823,522 at March 31, 2012.

Finally, Total stockholders' equity as revised would be $356,209 at March 31, 2012, a decrease of $279,867 from that originally reported of $636.076, or 44.0%.

Accordingly, should better proof of delivery and customer acceptance be unavailable, the above suggested changes would be material to the financial statements as originally issued.

The Firm also recognized that based on resolution of the revenue recognition issues related to the year ended March 31, 2012, the Issuer should be (and was) advised that the Firm would need to review similar information concerning amounts recorded related to revenue recognition in the interim reviews made by it for the quarters ended June 30, 2011, September 30, 2011 and December 31, 2011 10Q's in the year ended March 31, 2012; and the quarter ended June 30, 2012 10Q.

Issuer B engaged a successor PCAOB Registered Firm to review its interim quarterly financial statements for the 9/30/2012 and 12/31/2012 10Q's of Issuer B, in which Issuer B adopted the "cash basis" of accounting for revenue recognition, although it did not reflect any deferred revenue liability representing partial payments for software that was undelivered to or not accepted by the customer.

In very late July/early August 2013, in conjunction with the successor in the process of performing their audit of Issuer B's financial statements for the year ended 3/31/2013, Issuer B contacted my firm and engaged it to perform the due diligence necessary to reissue the Firm's Auditor's Report on the restated financial statements for the year ended 3/31/2012, as well as for the interim reviewed 10Q quarterly financial statements for 6/30/2011, 9/30/2011, 12/31/2011 and 6/30/2012.

Due to Issuer B's having limited internal personnel with the skills, as well as there being insufficient time available to devote to assisting them by their independent financial advisor, information required by my Firm for the due diligence developing fresh accounting to make these restatements has taken several months more than may have been expected for this type of project, which also includes a required retest by the Issuer/Preparer of the related Software Intangible Assets and Goodwill recorded at 3/31/2012 associated with the product since the original tests and evaluation are impacted by the restatement of revenue recognized. Based on the limited personnel of Issuer B and its limited independent financial advisor's time to assist, there has been unavoidable additional time delays in the meaningful retest by Management for re-evaluation by my Firm as the auditor after completion of the retest by Issuer B.

Since the restated 3/31/2012 financial statements are expected to be included within the seriously delinquent 3/31/2013 10K alongside the financial statements for that year audited by a successor to my Firm, there has also been time involved in communications between the 2 Firms and the Issuer/Preparer concerning consistency of both accounting and disclosures that should be made in the financial statements and notes to be included in the current 10K that will be filed simultaneously with the amended filings for the year ended 3/31/2012 10K and the related amended filings for the 4 amended 10Q's.

I am hopeful that, based on the progress of due diligence work by the Firm related to all periods requiring restatements by Issuer B, that Issuer B will soon finally make the necessary filings, since there are only a couple of issues to be resolved. The Firm needs to invest the additional time to assure that restatements when filed by Issuer B are likely to be reliable.

The failure to perform sufficient procedures to evaluate intangible assets for impairment;

Response:

The Firm does not agree with the Inspection Team's assertion that the Firm failed to perform sufficient procedures to evaluate whether the amortizable intangible assets were subject to impairment in accordance with AU 342, Auditing Accounting Estimates ("AU 342").

In providing the Inspection Team a package of work papers on June 24, 2013 for this engagement, the Firm apologizes for the poor print quality of the intangible assets impairment evaluation work paper. We understand that the work paper may have been difficult for the Inspection Team to read, in particular concerning the "Legend "outlining the information used in the evaluation of the impairment test, which impairment test was prepared by the Issuer. The work paper related to the impairment test on this Issuer presented to the Inspection Team did not contain tick marks or source documents to demonstrate to where and how key information had been verified by the Audit Staff on this engagement. The Inspection Team reviewed another Issuer's engagement work papers during this audit, in which we are sure the tick marks and source information reviewed in the evaluation of the intangible assets Issuer impairment test was better evidenced. It should also be noted that the applicable work papers provided the PCAOB are clearly labeled "PBC".

As a result of Firm discussions with the Inspection Team, the Firm re-reviewed the evaluation, including the work papers provided to the Inspection Team to ascertain whether the assertions made concerning:

> "There was no evidence in the audit documentation ..... that the Firm had evaluated the reasonableness of the significant assumptions, including the sales growth rate, the gross profit rate, and the expense growth rate, used in the issuer's undiscounted cash flow analysis."

have any merit.

On July 2, 2012, the contract engagement partner for this issuer (Fred R Goldstein CPA) sent an e-mail to the PCAOB Inspection Team that contained attachments in which, among other things, stated:

<u>Intangible Assets Evaluation</u>

Attached is my copy of the (Issuer B) Intangible Asset Impairment evaluation, which may be easier to read than the copy provided to the PCAOB Team. The team has prepared a Comment concerning the assumptions used as evaluated in the Legend on the copy of my original schedule in my file that I faxed to the MTS CPA PC office today for that purpose. I reviewed my original to refresh on what I had the Audit team to do evaluated the Issuer's Impairment Test.

Please note that MTS 7/13/2012 in the lower right of the w/p is my way of keeping track that I received the e-sent schedule from Mike Studer or one of his staff.

In particular, I focused on the 6% rate of increase in SGA; and the 10% revenue growth rate. The attached Excel is a current synopsis of the 6% rate of increase in SGA as it was evaluated by me on 7/13/2013. In that Excel, you will also see that I expected a flattening of revenue growth in line with growth from 3/31/2011 to 3/31/2012 per the financial statements, at a level attained after 31% revenue growth induced by $806K of advertising in y/e 3/31/2011 followed by advertising of $354K in y/e 3/31/2012. The clearer copy I have provided to you shows how the gross profit rate was evaluated. I am hoping that the PCAOB Team will consider what has been provided in evaluating whether it believes the Comment is still appropriate.

On July 13, 2012, the Firm's Freeport Audit Staff confirmed the contract Engagement Partner's request to:

> "Create a pdf in which you sign and date it as preparer dated today. ...Attach this e-mail as my approval as engagement partner of the results ...."

The Firm currently prepared an Intangible Asset Impairment Analysis P&L Trends Related to the MTS CPA Evaluation ("Evaluation Analysis") from information it had available to it embodied in the filed 10K's audited by the Firm for y/e 3/31/2012, 3/31/2011, and 3/31/2010. While it may not be well documented in the work papers for the 3/31/2012 impairment evaluation, the Audit Team considered it at the time the evaluation was done. The Evaluation Analysis also contained information abstracted from the 6/30/2012 10Q Firm interim review from the filing posted on SEC EDGAR. Below are some observations that were true when the evaluation was made, and known to the Audit Team even if they could have been better documented:

1. The impairment evaluation took place before the Issuer agreed to reverse a $198K receivable/revenue recognized in y/e 3/31/2012. Apparently, the impairment analysis gross profit in y/e 3/31/2012 of $2,120K was not reduced to $1,922K as finalized in the 10K as filed. However, the Exhibit has been laid out to show that the Gross Profit % for the average of the 2 years 3/31/2012 and 3/31/2011 was in fact 46% before and 45% after the revenue reversal. The impairment test by the Issuer used 46.58%. We believe that the Firm did evaluate the Issuer's Gross Profit %, and it was found to be reasonable in the Firm's professional opinion. The interim 3 months ended June 30, 2012 produced an unaudited Gross Profit % of 44%.

2. The entities that comprise Issuer B that generate its operating revenues have been in operations, in substance, since the year ended March 31, 2009, a short track record in years that has witnessed sharp sales growth in the year ended March 31, 2010 that began to level off between the year ended March 31, 2011 to the year ended March 31, 2012. The Firm's Audit Staff was aware of this when the Issuer's impairment test was evaluated. As noted in the Evaluation Analysis, the revenue increased: 4% after the revenue reversal of $198K (Customer 4); 8% before the revenue reversal; but averaged 14% for 2 years ended March 31, 2012 and March 31, 2011. The revenue reversal related to a large contract where the Firm understood that there might have been difficulties in satisfying the customer that the products installed were precisely working according to specifications. With that in mind, the Firm assessed that 10% growth was attainable by the Issuer. Had no difficulties been encountered for this one customer, revenues would have increased by 8% from March 31, 2011 to 2012.

3. Operating expenses, excluding stock compensation, amortization of intangible assets, and advertising, increased by 6% from the year ended March 31, 2011 to the year ended March 31, 2012 as reflected in the Evaluation Analysis. The average increase in operating expenses, excluding stock compensation and amortization of intangible assets, and advertising, as indicated in the Evaluation Analysis was 5% for the 2 years ended March 31, 2012 and 2011. The Firm believes that its professional judgment concerning the Issuer's use of 6% was properly evaluated by us and the rate of expense growth was reasonable. While the 3 months 6/30/2012 10Q interim results might suggest a lower rate of operating expense growth, the amounts for the 3 months results are likely to vary somewhat from quarter to quarter, so the Firm remained confident that the 6% increase still had merit after the Firm reviewed that quarter's 10Q results.

In an attachment to the July 2, 2013 e-mail to the PCAOB Inspection Team, the contract Engagement Partner noted:

"GOING FORWARD - PRIOR ADVERTISING TO BUILD VOLUME ATTAINED - MODEST REVENUE GROWTH GOING FORWARD"

The Firm called attention to the fact that as advertising declined from $806K incurred in the year ended March 31, 2011 to the $354K level incurred in the year ended March 31, 2012, the trend in revenue growth peaked at 31 % in the year ended March 31, 2011, and then flattened to 8% in the year ended March 31, 2012 (before the revenue reversal of $198K), suggesting growth rate in the range of 10% was reasonable.

The underlying data used by the issuer were its recent historical financial statements (which were audited by the Firm).

Issuer C

(1) *The failure to perform sufficient procedures to test the allowance for doubtful accounts.*

Response:

On October 27, 2011, the Securities and Exchange Commission ("SEC") sent the Issuer a routine inquiry letter relating to the Issuer's December 31, 2010 Form 10-K. In the letter and subsequent correspondence concluding July 26, 2012, the Issuer's revenue recognition policies and reserve for allowances, returns, and doubtful accounts methodology were discussed.

In its initial October 27, 2011 letter, among other things, the SEC made the following comment:

1. "Your accounts receivable has increased at a rate faster than sales. For example, days' sales in accounts receivable was 25 days, 55 days, 123 days and 96 days at December 31, 2009, December 31, 2010, March 31, 2011 and June 30, 2011, respectively, based on respective

quarters then ended. Provide us proposed disclosures to be included in future filings explaining why accounts receivable has increased at a rate faster than sales and, if applicable, why collection periods exceed your standard credit terms. Also explain why an increase in the allowance for doubtful accounts in line with the increase in accounts receivable was not necessary."

The Issuer explained to the SEC that the reserve was set at an amount that is equal to at least the amount of accounts receivable at the balance sheet date projected to be uncollected at the end of the Company's next fiscal quarter multiplied by its gross profit percentages, essentially deferring income at the balance sheet date related to excess product that may have been shipped by the Issuer to and still held by its distributors. In a memorandum sent to the Issuer on March 30, 2011 (prior to the October 27, 2011 SEC letter), the Firm addressed the revenue recognition and reserve methodology issues and advised the Issuer that the SEC may in the future request revisions to the Issuer's accounting policies regarding these matters.

In a follow-up letter dated January 6, 2012, among other things, the SEC made the following comment:

2. "You state in your response to our comment one "The Company's accounts receivable reserve for allowances, returns and doubtful accounts is set at an amount that is equal to at least the amount of accounts receivable at the balance sheet date projected to be uncollected...multiplied by its gross profit percentage, essentially deferring income...related to excess product shipped by the Company...still held by its distributors. This methodology does not appear to comply with U.S. GAAP. If a transaction fails to meet all of the conditions of ASC 605-15-25-1 and ASC 605-15-25-3, no revenue or cost of revenue may be recognized until those conditions are subsequently met or the return privilege has substantially expired, whichever occurs first. Simply deferring recognition of the gross margin on the transaction is not appropriate."

As it turned out, the resolution of the issue turned on whether the "sell through method" for revenue recognition was appropriate or whether the Company should recognize revenue based on having met all the criterion under U.S. GAAP to do so.

In the Company's response dated February 3, 2013 to the SEC, among other things, the Company explained:

> ..."Sales terms provide for ...and generally do not include any right of return. As discussed...the Company's distribution agreements provide for inspections by the buyer of the quality of the product on delivery and resolution of any defects in quality with the Company. The Company does not have a significant history of returns or credits due to quality...."

In response to another SEC Comment 1. concerning MD&A, the Company advised the SEC:

> "The Company does not have a recent history of needing to make provision for doubtful accounts due to significant write-offs of uncollectible accounts receivable."

Commencing with its audit of the 12/31/2009 financial statements, the Firm began to perform enhanced sales cut-off procedures, and review extensively subsequent accounts receivable collections in order to gain an understanding of whether the Company's revenue recognition policies, and the methodology applied in setting a reserve for allowances, returns and doubtful accounts made sense, and were in accordance with the dictates of U.S. GAAP. The Firm explained this in a response to a PCAOB Draft Report of Inspection provided us on May 16, 2012 in which the Board had indicated the Firm's failure to perform sufficient procedures to test the allowance for doubtful accounts of this Issuer. The same reserve of approximately $1,000,000 also existed at December 31, 2009 - $1,006,597 as presented in the Company's audited Balance Sheet which reflected a net receivable of $2,283,257 (based on gross accounts receivable of $3,289,854). With that in mind, the Firm continued to monitor the reserve without having the Issuer go back to the principal year of origin of the reserve, and determining how it was set at that time. Among other things, that might prove costly and time consuming in terms of audit and accounting fees and time incurred by the Company's internal personnel. The Firm made that decision based on evaluating the key metrics in the financial statements at December 31, 2009, and in subsequent quarters in the year ended December, 31, 2010, including at December 31, 2010 in the annual audit performed by the Firm. In particular, the Firm was mindful of the growing accounts receivable balance during 2010, and the deterioration in the days outstanding, and that is why it communicated with the Company about it prior to the issuance of the audited financial statements for that year in the December 31, 2010 10K, and again in its routine communication to the Company's Board as required by professional standards subsequent to the issuance of those financial statements.

On June 22, 2012, the SEC sent a comment letter to the Issuer and expressed their belief that the reserve set aside for product sales remaining in the distribution channel was not necessary and that the December 31, 2010 Form 10-K/A filed April 15, 2011 should be amended accordingly (which the Issuer did on July 23, 2012). The effect of the restatement adjustments was to increase accounts receivable and retained earnings by $1,004,027 at December 31, 2010 (approximately 2.2% of previously reported stockholders' equity of $45,172,511) and to decrease net income by $29,708 for the year ended December 31, 2010 (approximately 0.3% of previously reported net income of $11,790,975). The SEC, in accepting the Company's restatement, did not request the Company restate years prior to January 1, 2009, when the reserve arose, because it apparently agreed that results prior to January 1, 2009 reported in Form 10K's by the Issuer were not significantly impacted to merit restatement of those back years. That is because as stated by the Company in its response of February 3, 2012 to its Comment 2:

> "In 2007, we increased the reserve for allowances, returns and doubtful accounts by approximately 5,826,225 RMB ($767,139 at an exchange rate of $0.13167 average exchange rate for 2007) to approximately 6,117,695 RMB ($838.761 at the December 31, 2007 exchange rate) to essentially defer the gross profit impact of estimated excess product in our distribution channel. In 2008, 2009 and 2010, the aforementioned reserve was adjusted to 6,678,362 ($979,700 at the $0.14669 December 31, 2008 exchange rate), 6,880,362 ($1,006,597 at the $0.14630 December 31, 2009 exchange rate), and 6,626,366 ($1,004,027 at the $.015152 December 31, 2010 exchange rate), respectively.

The Issuer further stated in that response:

> "Based upon our retrospective review of accounts receivable data for the years prior to January 1, 2009, that portion of the increase in the provision for reserve for allowances, returns and doubtful accounts in 2007 and 2008 related to deferral of the gross profit impact of estimated excess product in our distribution channel was no longer required at December 31, 2009, given our success in collecting accounts receivable outstanding subsequent to December 31, 2008."

It is our understanding from a Wall Street Journal article that it can take 8.5 months for the SEC and a filing Issuer to resolve a complex issue, such as the one involved with this Issuer. The Firm has a myriad of e-correspondence and attachments it assembled in gaining a re-understanding of the Company's policies and procedures, and reviewing translated documents such as purchase orders, delivery tickets, distribution agreements and collection policies, as well as evidence that the Company extended its payment terms to 90 days without doing anything that might suggest "sell through accounting" was appropriate. However, the Firm thought it prudent to await communication with the Issuer by the SEC before suggesting the Company change its revenue recognition policy or the method in which it determined its reserve for allowances, returns and doubtful accounts. That said, the Firm does not understand why the PCAOB felt it was necessary to identify this as a deficiency. After all, the Firm recognized both the points raised in the past by the PCAOB, and carefully revisited the facts and the relevant accounting literature once the SEC clarified the issues related to U.S GAAP. The Firm believes it did what was appropriate concerning this reserve in the circumstances.

We appreciate this opportunity to respond.

Respectfully Submitted,

Michael T. Studer
President