American Corporate Counsel Association
Corporate and Securities Law Committee
Washington, D.C.

June 30, 1999

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: File No. S7-30-98: The Aircraft Carrier Release

Dear Mr. Katz:

We are a task force of the Corporate and Securities Law Committee of the American Corporate Counsel Association. We are responding to your request made in Release No. 33-7606A for comments on your proposals to change the regulatory structure for securities offerings.

ACCA is a national bar association made up of more than 10,000 attorneys who practice law as members of corporate law departments. Our Committee has more than 2,500 attorney members, a large number of whom practice securities law as in-house counsel for public companies. As such, our Committee is well situated to comment on the Commission's proposals.

Our letter has been circulated for comment among the leadership of our Committee and certain other members of ACCA. Although this letter contains the considered judgment of the Committee's leadership, ACCA's board of directors has not reviewed it and thus it is not an official position of ACCA.

Generally

We support your efforts to modernize the regulations governing the offering and sale of securities. We endorse many of the proposals in the release and recognize the numerous benefits intended to be offered by the proposed changes, such as:

• Increasing information flow to investors by allowing more issuer communications and making disclosure more timely;

• Reducing costs and risks of the registration process by giving issuers more certainty and eliminating outmoded requirements such as final prospectus delivery where it is irrelevant;

• Increasing the quality and usefulness of Exchange Act reporting; and

• Curtailing formalisms that impede capital formation, such as the "metaphysics" of public and private offerings.

In some respects, we think the proposals are broader than necessary and may create costs and burdens for responsible issuers that cannot be justified. Our main suggestions to improve the proposals are:

• Keeping the existing S-3 shelf in place. It currently works extremely well. It can be preserved without losing any significant benefit from the proposals.

• Allowing issuers that currently qualify to use Form S-3 shelf registrations to be able to continue to use a short form registration. Abuses, if any, have been far less significant than the benefits to issuers and to our markets as a whole.

• Phasing in the free writing proposals to allow the issuer and investment banking communities to assess the new communications mode and the potential liabilities relating thereto. Ideally, the issuer would be responsible for and would have the ability to control free writing communications. By limiting the use of free writing and creating accountability, the Commission could monitor and limit abuse in the experimental phase. With adequate controls in place, the Commission could forego requirements to file all free writing during the offering period, which may be impractical.

• While we support improvements in Exchange Act reporting, some proposals are based on an impractical view of what directors and officers should be doing or impose burdens on issuers without corresponding benefits to the public. This is particularly true of the proposals requiring formalistic director and officer signatures or certifications. We also think that the proposals to mandate filing of the quarterly and annual financial information described in Item 301 of Reg. S-K in an 8-K and to accelerate the due dates for 10-K and 10-Q reports offer minor benefits to investors but will force many issuers into either non-compliance or the filing of reports with less reliable disclosure.

We urge the Commission to consider adopting portions of the release which could be of great benefit on a stand-alone basis, such as those relating to the integration of and switching between private and public offerings, and certain Exchange Act proposals such as shortened filing periods for 8-K reports. We also believe the Commission should consider whether other parts of the release that

may very well benefit from further analysis and comment should be re-proposed, such as coordinating the new Form B registration scheme with the current Form S-3 shelf registration system and establishing the appropriate parameters for expanded free writing.

The Offering Process

Eligibility: Mechanics; Disqualifications

While we generally endorse the new Forms A, B and C proposed in the release, we believe that all issuers who currently are eligible to use Form S-3 for shelf registrations should continue to be able to do so in parallel with the new forms. From the adoption of Rule 415 in the early 1980's, the shelf registration process has provided issuers with an efficient and cost-effective way to access the capital markets, and this financing mechanism should not be discarded without substantial evidence of abuse.

We believe some of the proposed offering mechanics for Form B issuers, including the requirement to deliver a term sheet prior to an investment commitment, to file the entire prospectus prior to sale, and to file all free writing materials, have the potential to significantly slow down the timing of offerings and impede the rapid access of issuers to volatile market windows currently afforded by the shelf registration process. Any such delays will increase transactional risk and most likely will result in higher costs to issuers. These delays will be particularly problematic and unnecessary in transactions such as investment grade debt and medium term notes sold off the shelf, where the key considerations for the investment such as credit rating and interest rates can be easily communicated orally without the necessity of a prospectus or term sheet. We also note that the shelf system is generally bolstered by the efficiency of the securities markets and strong analyst followings for many S-3 issuers, which results in virtually instantaneous information flow about these issuers to the benefit of prospective purchasers in shelf offerings. We respectfully submit that the current shelf system in most instances is working extremely well for both issuers and investors and should not be abandoned without more evidence of abuse.

With respect to the proposed Form B registration system, to streamline the process so it provides some of the efficiencies of the S-3 shelf system, the Commission could consider exempting from pre-commitment delivery requirements those transactions where investment decisions can be easily made based on oral communications about the key terms of the deal, such as investment grade debt and medium term notes, or where the most relevant information will be contained in Exchange Act reports, as in the sale of common

stock. In addition, in lieu of pre-sale filing of the entire prospectus, the Commission could consider requiring a press release announcing a securities offering to be issued around the time of pricing, and allow the full prospectus to be filed within 48 hours of pricing similar to current requirements. We note, however, that many types of securities offerings will not be material to investors generally, such as investment grade debt deals having no significant implications to the issuer, and we believe no press release should be required in connection with such transactions.

We also believe some of the proposed disqualification provisions for use of Form B should not be adopted. The "bad boy" disqualification would, in too many instances, be draconian and disproportionate relative to the infraction. For example, if an offering participant has a disqualifying violation unbeknownst to the issuer, it would seem unreasonable in these situations to deprive an issuer of the use of the abbreviated Form B and faster access to the markets. Similarly, we do not believe issuers should be disqualified from using Form B because of an outstanding dispute with the staff regarding comments on Exchange Act reports. This proposal would hold any offering hostage to the staffs comments, irrespective of the merits or materiality of such position. Because issuers generally would not be willing to risk a Section 5 violation in the face of unresolved comments, this proposal could render illusory the automatic effectiveness of Form B registration statements. Both "bad boy" violations and issues being disputed with the staff can be addressed through other traditional enforcement mechanisms and more specific disclosure requirements to the extent this type of information is considered material and not already required to be disclosed.

We also believe it is important to maintain the presumption under Rule 401(g) relating to the proper use of registration forms. To the extent issuers cannot use a registration form with the comfort of knowing they are not violating Section 5, the attraction of declaring one's own registration statement effective will be drastically reduced. The Commission should maintain the presumption of eligibility at least in situations where forms are used in good faith by issuers, and employ stop orders, injunctions and other existing enforcement mechanisms where the use of a form by any such issuers ultimately proves to be inappropriate.

The Commission should also reconsider the proposed threshold for general availability of Form B. The proposed test of $250 million in public float or $75 million in public float and $1 million average daily trading volume will deprive a large group of issuers of short-form registration who currently are eligible to use Form S-3. We suggest that the Commission consider allowing all companies with a float of $75 million to use Form B, similar to the current threshold for use of Form S-3, without reference to average daily trading volume. Given the similarity

of Form B and Form S-3, and the additional protections built into the Form B offering mechanics, we submit the Commission should not be more selective in defining the eligibility of Form B users than that previously deemed appropriate for Form S-3. Retaining the current S-3 test would also create less of a burden under the proposals for issuers that want to use Form B for secondary offerings, but who would be precluded with a higher float test.

Free Writing

We applaud the Commission's proposals to allow issuers to more broadly communicate with investors during the pre-filing and offering period. The proposals have the potential to allow issuers greater flexibility in their sales efforts, accommodate the changing realities of information flow afforded by the Internet and emerging technologies, and reduce the prevalence of rumor and broker-dealer oral communications during the offering period. Expanding the safe harbors for analyst research reports will further facilitate productive communications during the offering period.

At the same time, we believe several aspects of the proposals should be modified. Free writing communications used during the offering period should not be filed with the Commission, nor should those materials be defined as part of the registration statement and subject to liability under Section 11. In addition, neither the issuer nor any other participant in the offering should be responsible for free writing materials that it has not created, used or approved. Under the proposals, the issuer and other participants would have to identify and track all communications made on their behalf during the offering period which would create significant costs and risks of liability in excess of the benefits to issuers. In short, it is unlikely many issuers would more freely communicate during the offering period under these proposals.

We suggest that the free writing proposals, in somewhat modified form, be permitted at first on a trial basis to allow the issuer and investment banking communities to develop the expanded communications in a more measured way. The new free writing rules could be made available to issuers of a certain size or reporting history, or to firm commitment underwritings of a certain deal size. The Commission could also limit free writing communications to those approved in writing by issuers so they are not responsible for the unauthorized use of, and can better control the quality of, materials by other deal participants. Liability should be applied to parties that actually create, approve or use the free writing material rather than imposing joint exposure for all deal participants.

As mentioned above, we do not believe free writing materials should have to be filed with the Commission. This would further delay the offering process and may prove to be a significant deterrent to communications during the offering period.

To the extent it must approve all free writing materials, the issuer would help ensure the accuracy of these communications. Issuers could be required to retain all free writing materials for a 5 year period and to post all such materials on their website (if any) from first use to closing of the offering. Investors could be informed in the prospectus of the availability of the free writing materials on the issuer's Web and for inspection upon request to the issuer.

We also believe other aspects of the free writing proposals should be refined. We fully support a defined pre-filing period outside of which communications would not be deemed free writing or offering materials. However, the proposed offering period for Form B issuers of 15 days prior to the first offer is too vague. A clearer line needs to be drawn or many issuers will not be willing to freely communicate during such an ambiguous period and risk a Section 5 violation. This period might commence 15 days prior to the filing of a registration statement, or for shelf registrations, given the rapid time frame of such deals, possibly 5 or 10 days prior to pricing. Issuers also will need more clarity on what constitutes ordinary business communications so they don't feel compelled to file the type of routine press releases that currently are not considered part of offering sales materials. For example, press releases discussing business developments that may refer to certain forward-looking information such as new product launches should not be considered free writing. The distinction between free writing and offering materials should also be defined more clearly.

Dividend Reinvestment and Stock Purchase Plans

Under current law, companies can generally use Form S-3 for their dividend reinvestment plans and direct stock purchase plans even if they do not have the public float to be eligible to use Form S-3 for their other offerings. The proposals offer the use of Form B for this purpose but would impose new ownership, issuance and purchase restrictions that would disadvantage issuers and participants in these plans without providing corresponding benefits to investors.

These plans allow companies to encourage shareholder loyalty and build relationships with customers and employees. Depending on the plan, investors may acquire newly issued shares or shares that were acquired by the plan on the open market. These plans are also the most economic way for small investors to own individual stocks and are a low-cost and flexible means for issuers to raise capital. Under the proposals, an issuer could register its plan on Form B only if the plan is offered to existing shareholders who held the stock for at least two months. We do not believe that this restriction, which is intended to assure that investors already have some familiarity with the issuer before participating in the plan, would benefit investors. Investors are not solicited to participate in these plans. They must first contact the issuer or its transfer agent to request a prospectus and enrollment materials. Since new investors in brokerage accounts

(which are subject to no such two-month limitation) are potentially subject to solicitation, we believe that any danger of investor abuse would be far smaller with stock plans than with brokerage accounts, not greater. It also might be difficult for issuers, transfer agents or brokers to measure the length of time that the investor held the shares.

The two-month holding requirement would deny the use to certain issuers of Form B for "direct purchase" plans, which currently may be filed on Form S-3. The proposals permit Form B to be used irrespective of the float of the issuer for offerings to existing shareholders. However, direct purchase or "open availability" plans allow investors to make their initial purchase of stock within the plan. From the investor's standpoint, these direct purchase plans are a convenient, low-cost way to buy shares directly from the issuer, since shares do not have to be acquired through a brokerage account and removed from that account to be deposited in a plan. From the issuer's standpoint, they are a flexible and efficient way to raise capital. Under the proposals, all direct purchase plans for sales to new shareholders would have to be registered on the more costly Form A. We believe that the proposed two-month holding period should be eliminated.

The proposals would also limit a company seeking the use of Form B to register no more than 15% of its public float when aggregated with the dollar amount of shares previously registered for sale to existing shareholders on Form B within the prior twelve months. This departure from current law would weaken the ability of issuers to use these plans as a low-cost, flexible method for raising capital. Currently, depending on market conditions, companies can offer securities through stock purchase plans in whatever amounts they determine. In the absence of known abuse, we believe the Commission should not restrict issuance amounts under these plans.

The proposals would also restrict the amount of purchases that a shareholder may make. Shareholders would be limited to the smaller of 100% of the value of the issuer's securities they own already or 5% of the total offering amount, except that the shareholder may purchase $10,000 worth of stock in the plan in any twelve-month period. Currently, plan participants are subject to no such restrictions. This proposed cap on purchases would limit the utility of these plans for investors and the flexibility of issuers in raising capital. Institutional investors would not be able to efficiently acquire shares directly from the issuer pursuant to a plan as they can and do today. These institutional investors are clearly able to fend for themselves without needing the additional disclosure of Form A. We therefore believe that these limitations on purchases are unnecessary and undesirable.

Integration of Private and Public Offerings

We believe the proposals that address solutions to integrated public and private offerings are extremely constructive and should be adopted, irrespective of the outcome of other proposals in the release. The interpretation of Rule 152 providing greater clarity when moving from a private to a public offering, and the cooling-off periods to commence a private placement following a public offering, will give large and smaller issuers greater flexibility in testing the waters and freer access to both private and public capital.

Exxon Capital

We understand the rationale for proposing a repeal of the staffs position in Exxon Capital, and acknowledge that analytically it may not fit perfectly into the regulatory framework. We note, however, that certain high yield and other issuers heavily rely on this method of capital raising, and outright repeal may very well impose significant additional costs on these companies.

Exchange Act Proposals

We fully agree with the Commission's view that accurate and reliable reporting under the Exchange Act is an essential predicate to an efficient and accelerated offering process. However, we believe the release proposes several changes under the Exchange Act which will not significantly improve the quality of disclosures, and in certain cases, are impractical.

Signatures and Certifications

We do not support the proposal to require additional officer and director signatures on 10-Q reports. As more informational demands, such as expanded MD&A disclosures, make timely filing of these reports ever more challenging, it would be impractical to expect a majority of the board of directors to review the 10-Q report in its entirety and in final form prior to filing. Nor do we believe this requirement would be consistent with the traditional role of directors, which is more appropriately to ensure that proper financial reporting processes and controls are in place rather than to perform detailed review and editing of the financial reports. In this regard, the board should be entitled to rely on management for the presentation and disclosures in 10-Q's to the extent sufficient internal processes are in place to ensure accurate financial and other disclosures in such reports. We also note that a requirement for directors to sign 10-Q's would go beyond the recommendations of the Blue Ribbon panel on audit committee responsibility, and suggest that any rules on director signatures await the conclusion of the Blue Ribbon initiative to ensure consistency in approach. Although we have less of an objection to the principal executive officer signing a 10-Q report than a majority of the board, we do not think this will improve the

quality of the disclosure, which already must be signed by the principal financial or accounting officer. In our experience, such officers provide thorough and detailed reviews of the 10-Q report.

We also believe requirements that directors and officers certify that they have reviewed Exchange Act reports (and Securities Act registration statements as well) and know of no material misrepresentations or omissions therein would not significantly increase the quality of disclosure in these reports. It is our experience that these reports are already read carefully by signing officers, as such officers have great incentive to be careful and diligent, given their own potential liability as signatories in both administrative and judicial forums and potentially massive fraud on the market liability for their companies based on materially inaccurate disclosures. Rather than improving the disclosure in Exchange Act reports, we believe the certification will most likely result in signing officers becoming targets in litigation more often, and possibly have a counterproductive effect in deterring qualified directors from serving public companies. The requirement could also impose extremely difficult logistical issues if changes are made at the last minute, as they frequently are, after board members have provided their certifications.

We do not oppose the requirement to have an officer certify that all 8-K reports have been sent to the board of directors, as long as the directors need not be sent or receive the reports before filing with the SEC. We endorse the purpose of keeping directors informed of key company initiatives, but as we expressed above with respect to 10-Q's, believe it is unrealistic and unnecessary to expect directors to provide a meaningful review of every 8-K filed with the SEC. In many instances there may not be sufficient time to notify directors of a fast-breaking development that is reported in an 8-K, and to require such review by directors would unnecessarily set up a standard that too easily could be exploited by the plaintiffs' bar.

8-K Requirements

We generally do not oppose the additional items that would be added to 8-K reporting requirements, nor do we object to a shorter filing period. However, we believe the filing requirement generally should not be less than 5 days after the event which triggers the report. This will give the issuer sufficient time to complete preparation of the report and EDGARize it for filing with the SEC. This process necessarily takes time to organize all internal parties, some of whom may not be immediately available, as well as third parties, such as auditors and counsel, if necessary. The time required to adequately prepare a report depends on various considerations, but any report due within one or two days after an event, even if it could be prepared quickly, might be very difficult to timely file if

necessary signatures cannot be obtained on a day's notice due to vacation or other reasons.

Although burdensome, a limited two business day filing requirement for 8-K reports might be feasible with respect to certain material matters. These could include the events proposed in the release for a one business day filing requirement, such as the resignation of a director, certain notices by auditors or defaults on senior securities. However, any such rule should apply only to the extent such events are material, which will not always be the case. For example, the fact that a director resigns for personal reasons might not have important implications to the issuer or be of significant interest to investors. We also note that to the extent a press release is issued on the day of a reportable event, a two day 8-K filing requirement could be more practicable because all internal fact-finding and drafting describing the event will have been completed, leaving only EDGARization to be done by the filing deadline. However, in certain situations, e.g., uncertainty why a director or auditor has resigned or a dispute regarding a material default, it could take two days or longer to gather all the facts, coordinate all relevant parties and prepare a disclosure describing the event that would be appropriate for release to the public. In these situations a two day 8-K filing requirement could be extremely onerous. If a two day requirement is adopted, there should be some relief for issuers who act in good faith but fail to timely file due to the need to gather facts or EDGARize a disclosure document or for some other legitimate reason.

Reporting Quarterly and Annual Results

We would support a rule to require all material press releases issued by public companies to be filed with the SEC on an 8-K report. This may very well help avoid selective disclosure issues by ensuring greater access to such information by all investors. However, as discussed above, we believe the Commission should allow sufficient time after the issuance of a press release for an issuer to EDGARize the materials and file them with the SEC.

We also do not believe the financial information in the press release or 8-K should have to conform to Item 301 of Reg S-K. Many small issuers do not have the resources to prepare this financial information in the requisite time frame, and even large issuers would probably begin reporting earnings later than their current schedules due to the need to apply the type of analysis required by Item 301 of S-K, which in some respects is similar to the MD&A. We believe the Commission should allow the market place to shape the disclosures issued in press releases, which may very well vary due to the industry, size of issuer and other considerations, and have any such releases, if and when publicly issued, filed on an 8-K to address selective disclosure issues.

Acceleration of 10-Q's and 10-K's

As described above, we support the filing of press releases reporting earnings on an 8-K report. We also would support due dates for such filings no later than 30 days after the end of a quarter or 60 days after the end of the year.

At the same time, we do not support the proposal to accelerate the due dates of 10-Q and 10-K reports to within 30 days and 60 days, respectively, of the quarter-end and year-end. Although we understand the Commission's concern about information becoming stale, as a logistical matter, many issuers are already pressed to file these documents on a timely basis, primarily due to the time it takes to properly prepare the MD&A and have it adequately reviewed by all relevant internal and external parties. Further acceleration of due dates might very well force issuers to cut corners and would have the potential to lead to increased inaccuracies. These pressures obviously would be compounded by some of the additional requirements proposed in the release, such as having a majority of directors sign the 10-Q and certify as to its accuracy. However, to the extent the Commission decides to accelerate these deadlines, there should be at least a one-year grace period before the proposal becomes effective so issuers will have the opportunity to adjust their reporting processes to account for such change.

Management Audit Report

We agree with the Commission's view that the audit committee should play an important role in connection with an issuer's financial reporting system. We also acknowledge that there could be some benefits from a report by management to the audit committee describing the procedures in place to ensure accurate reporting by the Company. However, any such report filed as an exhibit to the 10-K may be a target for litigation, may ultimately end up being a boiler plate set of procedures not necessarily reflective of the differing needs of various issuers, and may not be necessary if other measures are taken to ensure the audit committee participates in and is assured of proper disclosure procedures at a company. We urge the Commission to await the outcome of the Blue Ribbon panel recommendations to determine if additional measures to ensure proper audit committee involvement in the process is really necessary.

Risk Factors

We do not object to some type of risk factor disclosure in the 10-K, with updates of material changes in a 10-Q. However, we note that the release proposes risk factor disclosure that is very different from the requirement under Item 503 of Reg. S-K applicable to prospectuses, Item 303 of Reg. S-K applicable to the MD&A, and the Private Securities Litigation Reform Act safe harbor for forward-

looking statements. Item 503 calls for information that would make an offering risky, and Item 303 requires disclosure of information that would be reasonably likely to materially impact the results of operations, liquidity or capital resources of an issuer. The proposals would impose yet another requirement for disclosures of risks that may negatively impact the future financial performance of an issuer, but seemingly without any probability or magnitude thresholds. This could result in issuers trying to identify every possible risk that could have an adverse impact on their business, and boilerplate risk factors might very well follow. Such disclosure would not be of great value to investors.

The proposed risk factor disclosure would also seem inconsistent with the safe harbor for forward-looking statements contained in the Litigation Reform Act, which provides protection for forward-looking statements that are accompanied by some important, but not necessarily all, risk factors relating to such statements. Because a practice has already developed among many issuers of making risk factor disclosures in Exchange Act reports that qualify for safe harbor protection under the Litigation Reform Act, we suggest if any additional regulation in this area must be adopted, that the Commission consider a rule that requires mandatory, rather than voluntary, compliance with the safe harbor.

<u>Review of Exchange Act Reports</u>

We fully support the proposal to provide issuers more guidance as to the timing of their Exchange Act reports.

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In conclusion, we support the Commission's efforts to modernize the securities offering process, and endorse certain of the proposals contained in the release. However, we believe the Commission should seriously consider revising some of the proposals which, as mentioned above, do not seem to offer significant benefits, or address serious threats, to investors, and in some cases are not practical. The Commission should adopt certain proposals without further comment, such as those providing greater clarity and flexibility in switching between private to public offerings, and possibly several proposals under the Exchange Act, such as shorter periods for filing of 8-K reports. We also believe the Commission should consider whether portions of the release should be re-proposed that may very well benefit from further analysis and comment, such as the coordination of the new Form B registration with the current S-3 shelf registration system and the parameters of expanded free writing.

Please direct any questions relating to this letter to Richard Starr (212-640-5785) or Joseph Heyison (201-447-9000).

Respectfully submitted,

The Corporate and Securities Law Committee,
American Corporate Counsel Association

By:
Richard Starr
Vice Chairman

cc: The Honorable Arthur Levitt, Chairman
The Honorable Norman Johnson, Commissioner
The Honorable Isaac C. Hunt, Jr., Commissioner
The Honorable Paul R. Carey, Commissioner
The Honorable Laura S. Unger, Commissioner