REMARKS OF RICHARD B. SMITH, COMMISSIONER,
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AT SEMINAR OF THE FEDERAL BAR ASSOCIATION IN
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THE PUBLIC INFORMATION ACT AS IT AFFECTS THE SEC

I would like to preface my remarks by pointing out that, since I am only one of five members of the Commission, my views on the proper application of the Act to certain areas are not necessarily those of the full Commission. However, as partial compensation for your inability to cite me, I would also point out that I have only recently joined the Commission from private practice, so that my remarks will undoubtedly reflect something of my background as a private practitioner rather than a career government employee.

In this connection, one of the Commission's career attorneys who worked in implementing the Act referred to it, in an apparently Freudian slip, as "The Freedom _from_ Information Act." I am, of course, taking the position that disclosure of his name would constitute "a clearly unwarranted invasion of personal privacy."

His remark though does reflect his background with our agency. While not without our problems, I would venture to guess that the Act has had less impact upon our Commission than upon almost any other agency. This is so because the basic theme and thrust of the major statutes which the Commission administers is full disclosure.

Most of the material in our files is public, and we attempt to have it readily available to the press and to individual members of the public. Our rules of practice provide that documents filed with the Commission are public unless otherwise provided by statute or rule, or directed by the Commission. Thus to some extent the general presumption for the government created by the Information Act to a marked extent already existed in our agency. We attempt to assure wide dissemination of our rule proposals, rules, decisions, opinions and statements of policy, as well as releases that reflect interpretations of key provisions of the statutes. We do this by furnishing copies of the material to

the press, by making it available for public inspection in all of our offices, and by sending copies to the many persons on our mailing lists. Further, both the Commission and its staff are available for discussions with individuals or corporations as to the application and coverage of the securities laws. I am sure we can improve further in these areas, but I think the Commission's record, even prior to the Public Information Act, is in general a commendable one.

Obviously, therefore, we are in complete sympathy with the purposes of the Public Information Act. We have been actively engaged in implementing not only its letter but, we believe, its spirit. On June 30th we adopted a comprehensive amendment to our long standing rule governing the public availability of material in our files. The amendment established procedures for making and handling requests for information under the Act and provided for administrative review of any denial of information. Appended to this rule is a list, in general terms, of the various documents available from the Commission.

We are considering further steps in keeping with the spirit of the Act (although not necessarily required by it).

(1) We are giving consideration to issuing periodic releases of important and novel determinations which are cleared by the Commission and expressed either in no-action positions or interpretations. (I shall describe "no action" later.) Such releases would contain generalized statements which would be free of identifying details. Personally, I would also hope that we could publish a release setting forth the more important and useful Commission interpretive positions predating the enactment of the statute and heretofore not made public. We are also considering making staff interpretive letters and no-action letters available in our public reference room with identifying details deleted. We are considering whether guidelines might be adopted for making the full text of such letters available after substantial time periods have elapsed, and confidentiality may have become a factor of little importance.

(2) We had already published in booklet form a compilation of the more important releases dealing with matters frequently arising under the Securities Act of 1933, and we propose to do this under other statutes administered by the Commission. Early this year we issued an extensive release explaining the Commission's net capital rule in simple language for use by affected persons.

(3) Also under consideration is a proposal to place certain Commission briefs in bound volumes in the public reference room and to index them.

(4) We had also published, in 1964, certain guidelines for preparation of registration statements which the staff had evolved over the years. These are currently undergoing revision and supplementation by the staff and a more extensive compilation will be released soon.

As you can see, we are attempting to find ways to make available as much information as we possibly can, but we would do so without unduly interfering with the privacy of those who are subject to our regulation. A statute phrased in as general terms as the Public Information Act is inevitably subject to differing interpretations, especially when it seeks to reconcile such divergent purposes as

> "the right of the public to know and the need of the Government to keep information in confidence to the extent necessary without permitting indiscriminate secrecy."

I would like to address myself to three areas in which the Commission has applied the statute and made a determination as to the applicability of an exemption and to outline why I think these decisions have been proper ones. These areas are:

(1) Staff no-action letters and interpretations;

(2) Letters of comment under the 1933 and 1934 Acts and preliminary proxy material; and

(3) Intra-agency memoranda.

Before launching into these subjects, however, I would like to say that I believe the spirit of the Act also serves to deal with a problem which I don't believe is expressed, at least directly, in the literature on the Act which I have read. That is the complaint occasionally made about administrative agencies, and which which I believe such agencies must always be on guard against, that the specialized bar practicing before it has information available to it that is not available to the average practitioner. The specialized bar would include alumni of the agency and other lawyers with considerable experience in dealing with the agency. It is perhaps inevitable that an administrative gloss will adhere to any agency's rules and forms and interpretations and procedures -- a gloss that is not readily determinable, or not at all determinable,

from the published requirements. It is also perhaps inevitable that lawyers who deal with an agency and work in a particular substantive area exclusively, will obtain a facility in handling such matters that a lawyer less experienced in the specialty could not hope to acquire. Nevertheless, despite this inevitability, I believe it an agency's obligation to reduce to a minimum the chances that any particular group of practitioners will gain a monopoly on representation before the agency. I believe that the spirit of the Public Information Act goes to this concern. The steps the Securities and Exchange Commission has under consideration to make interpretive and no-action letters generally available, to prepare and disseminate up-to-date staff manuals, to issue guidelines specifying particular applications of general language of the statutes and rules, and the staff's and Commission's long practice of holding themselves available for consultation -- these steps I believe go and have gone some distance toward placing specialists and the general practitioner on an equal footing before the Commission, at least to the extent that all the basic rules are known to both.

Of course, with the burgeoning interest throughout the country in securities law and the wide range of companies registering securities for sale to the public, "specialists" are now appearing all over the country. Moreover, sometimes the general practitioner has an advantage over his metropolitan brother who is perhaps more sophisticated in securities matters. To illustrate this, let me read you two letters which the Commission's staff received several years ago from an attorney in a small town in Kentucky, I believe.

The first letter (with names altered) is dated in January, and is addressed to our Chicago Regional Office:

"Dear Sirs:

"Mr. John Smith, president of Lake City Auto Auctions, has handed me your letter of January 12 to which please refer.

"Now I set up the corporation for these fellows. They have bought themselves a lot and are aiming to put up a place where used cars are auctioned off.

"The boys' intentions were to sell stock only to used car dealers. I know this for a fact, because I set in on several of their meetings when

they started the corporation last September. Of course, I suppose they could sell stock to the public if they took a mind to. There is nothing in their charter forbidding it.

"Now I frankly tell you that I am a country lawyer. There are a dozen lawyers in this town, and I would not give two cents for what all of us put together know about Federal law. The reason is that each one of the regulatory or administrative agencies of the govt. has got its own books of rules and regulations and if a lawyer here had them he would be bankrupt from buying them. So, most of us gave up on Federal law long ago. All I've got is a $3 book on bankruptcy. If some poor fellow comes in with a Federal problem, I tell him to write his Congressman. There may be a copy of the Securities Act of 1933 in this town, but I don't know who would have it, and I sure don't.

"So, if the Lake City Auto Auction boys are doing something you don't like, you let me know what it is and I will tell them to quit it.

"I can't figure how you ever even heard of this outfit. I think their competitors must have written to you. Maybe you could also check on their competitors.

"Yours,

/s/ J.M.P."

The second letter is dated a month and a half later --

"Dear Sirs:

"I thank you for your letter of January 29.

"It <u>does</u> appear that the stock offering might not have been entirely intrastate, and that therefore registration is required. I have wended my way through all the material you sent me, and I think I fairly comprehend the substance of Release Nos. 4434, 4554, 4450, 4470, and the Securities Act of 1933. However, I must confess that the 'General Rules and Regulations'

is the most incomprehensible document that has ever come to my hand. When I graduated from law school, I got the highest grade on the state bar exam. I have an I.Q. of 137, and I still can't read this d----d thing and make any sense out of it. Couldn't you just send me some blank forms to fill out? Then we could do business.

"Yours,

/s/ J.M.P."

There is, of course, a germ of truth in our correspondent's comments. Our rules necessarily reflect the complexity and variety of available methods of financing and of the industry we regulate. We cannot always expect the uninitiated and unsophisticated practitioner to understand them without some assistance. But under our practice, an explanation is in the usual case only a telephone call or a letter away in the form of a no-action letter or an interpretation from the Commission's staff.

(1) Staff No-Action Letters and Interpretations

Since its inception, the Commission has stood ready to respond to requests from members of the public for interpretive advice on the application of the securities acts to their proposed transactions. This interpretive advice usually takes two basic forms: (1) informal advice of a senior member of the staff as to the applicability of the securities laws to a proposed course of conduct; or (2) an assurance by a senior staff member that no action will be recommended to the Commission, if the inquirer pursues the course of conduct outlined. The former we call interpretive letters. The latter, because of the unvarying language with which they are concluded, soon became known as "no-action" letters. Obviously, there is something of both in each. These informal opinions or positions are not binding upon the Commission as precedent in subsequently arising cases. Moreover, while the Commission has to the best of my knowledge never taken action in a situation where a responsible staff member has stated that no action would be taken (unless the facts do not conform to the representations made to it) such advice is no bar to an action initiated by a private party to enforce a civil liability claimed to arise from an alleged violation.

In a speech delivered in 1935, the then General Counsel of the Commission noted that a great deal of staff time was devoted, even then, to answering public requests for interpretations, a practice which had been inherited from the Federal Trade

Commission. In fact, so much time was consumed by this function that he stated his fear that the Commission would become a giant legal aid society. However, it was his opinion then, and it has continued to be the view of the Commission since, that this informal service to the bar and the public is an important aspect of the administration of the securities laws. It leads to preventive law, the prophylactic obtaining of compliance before the event. Certainly it is true that the Commission receives many requests for interpretations from over-cautious counsel, counsel who are fully conversant with the law and capable of rendering a confident opinion of their own recognizance, but who wish to provide their clients every measure of available protection. As a result it is undoubtedly true that the service has on occasion been abused. Also too artfully composed statements or out-and-out misrepresentation of the facts of a proposed transaction clearly abuse this service. On the whole, however, I am confident that the vast majority of the requests are submitted in good faith and motivated by a desire to insure full compliance with the law.

Professor Davis has taken us to task for not treating staff no-action letters and interpretations as "interpretations which have been adopted by the agency" under Subsection (b) of the statute. Subsection (b) requires that precedential agency interpretations and statements of policy be made available for public inspection unless an appropriate exemption applies. However, the fact is that they are not agency determinations. Staff action is not Commission action. There has been no delegation of authority to the staff in this area, and the staff itself is not an agency within the meaning of the Administrative Procedure Act. The reasoning stated in such staff communications is not binding upon the Commission in any precedential sense, and it would, in fact, be affirmatively misleading for the Commission to make such material available as agency precedent. Therefore, it is the Commission's position that staff interpretations are not covered by Subsection (b) of the Act.

However, there remains Subsection (c) of the statute which requires that identifiable records by made available upon request. This provision appears to require production of staff no-action and interpretive letters unless an exemption is available.

In my own view, the staff of the Commission in this and other areas is acting as a confidential counselor to the public. The private practitioner brings his problem to the staff in

somewhat the same way that a client brings his legal problems to his lawyer. The exemption in Subsection (e)(4) for commercial and financial information obtained from any persons, and privileged and confidential, whatever that really means, is intended to apply. As the House Report states, this exemption

> "would also include information which is given to an agency in confidence, since a citizen must be able to confide in his Government. Moreover, where the Government has obligated itself in good faith not to disclose documents or information which it receives, it should be able to honor such obligations."

Accordingly, our rule, in my view, correctly exempts from disclosure, and I quote,

> "Information obtained in connection with interpretive letters or no-action letters which is deemed to have been submitted in confidence unless the contrary clearly appears."

As you may be aware, businessmen and their counsel discuss the full details of proposed transactions such as mergers, acquisitions and financing plans with the Commission's staff, frequently substantially in advance of consummation of the transaction, so as to attempt to assure full compliance with the statutes the Commission administers. In connection with obtaining staff interpretive advice and no-action letters in this fashion, businessmen expect, and they have a right to expect, that their confidence in disclosing these matters in advance will be completely respected. Premature disclosure of such transactions still in the formative stages could have unsettling effects on the securities markets and be misleading to public investors.

If corporate officers and their counsel could not in complete confidence seek advice about contemplated transactions, the securities laws, effects of which may be subject to debate, they would not turn to the Commission for informal guidance. And the Commission would be trying to lock the barn doors too late.

Moreover, many requests for no-action letters, while not involving sensitive transactions, do disclosure personal information concerning financial and family problems which the correspondent would not wish to be a matter of public record.

Although Subsection (e)(4), by its terms, exempts only confidential information, not entire documents containing such information, the Commission does not believe that the Act requires it to edit documents, especially where it may not be apparent what items of information would be deemed obtained in confidence and where the document may not be meaningful after editing, as would often be the case with interpretive and no-action letters.

The Commission recognizes that even though the material is exempt under the statute, prior interpretive positions of the Commission and its staff would be helpful to persons planning or negotiating transactions. Accordingly, as I stated earlier, the Commission is giving active consideration to publishing in regular periodic releases its more important interpretations and no-action positions and to making them available in bound volumes in the public reference room of the Commission with an appropriate index, to the extent they are meaningful after deletion of identifying details.

However, the Commission must be careful not to compromise, in its attempt to provide as much meaningful information as possible, an informal process which has proven of great service to the bar and an indispensable alternative to formal enforcement of the securities laws. More harm than good would result if the publication policy adopted should discourage informal consultation with the Commission or its staff.

I should mention here and in other applications of the confidentiality exemption which I shall discuss, that the focus of the Commission's concern is upon the private party's interest in maintaining the confidentiality of the information submitted. If in any case the private party states that he does not require confidential treatment, the document in question is made freely available. In administering its rules where A asks for a document submitted by B which is deemed to have been submitted in confidence by B, the Commission staff has, on occasion, written or telephoned B to obtain his agreement, if possible, to make the document available. The Commission's stake in this matter is to protect the individual's privacy, not its own.

(2) Letters of Comment Under the 1933 and 1934 Acts and Preliminary Proxy Material.

In applying the confidentiality exemption in the area of letters of comment under the 1933 and 1934 Acts the Commission's rule exempts,

"Information contained in letters of comment in connection with registration statements,

applications for registration or other material filed with the Commission, replies thereto, and related material which is deemed to have been submitted to the Commission in confidence or to be confidential at the instance of the registrant or person who filed such material, unless the contrary clearly appears."

The registration statement under the 1933 Act is, of course, fully available for public inspection immediately upon filing. The purpose of the securities acts registration and reporting requirements are to make information publicly available. Specific provisions are necessary to grant confidential treatment to information disclosure of which may be injurious to the registrant. Accordingly, where a company believes that disclosure of provisions of a material contract required to be attached as an exhibit to a registration statement or report would impair the value of the contract or reveal trade secrets, it must make formal application for confidential treatment of such material. Even in these cases, the Commission must find that disclosure is not in the public interest or necessary for the protection of investors.

However, the written communications and conversations among the Commission's staff, the registrant and its counsel -- which are, in effect, intermediate negotiations in the course of developing the final and definitive form of registration statement -- are not made public. Information not specifically required is oftentimes given to the staff in confidence in order to assist the staff in evaluating the adequacy and accurancy of representations in the registration statement. Any inhibition upon this free exchange of information and ideas between the staff and the registrant could seriously impair the effectiveness of an informal procedure developed by the Commission over some 30-odd years and held up for praise by the Attorney General's Committee before passage of the Administrative Procedure Act, by the staff of the Hoover Commission and by other observers of the administrative process. Suggestions of the staff are normally accepted and lead to appropriate amendment of the relevant documents. This process might become very difficult, if not impossible, if such correspondence were to be made public.

Similar problems of supplemental information exist with respect to registration and reports under the 1934 Act. And here too the documents are available immediately for public inspection,

not only at the Commission, but also at any securities exchange on which the registrant's securities may be listed. The exchange may require additional information to be filed with them which is made available to the public.

Of course, registrants and their counsel do have a legitimate interest in the manner in which the staff is treating the registration requirements in its letters of comment. However, the way to satisfy that interest is not to disclose confidential information but to publish up-to-date and comprehensive Manuals of Practice. Both the legitimacy of the interest and the proper means of responding to it were recognized by the Commission in February, 1964, when it published Securities Act Release 4666 setting forth previously non-public staff guidelines for the preparation of registration statements. The Division of Corporation Finance is presently revising and supplementing these guidelines, and a more extensive compilation will be published in the near future.

Similar considerations apply to preliminary proxy material and the Commission's rule in this area exempts, and I quote,

> "Information contained in any document submitted to or required to be filed with the Commission where the Commission has undertaken formally or informally to receive such submission or filing for its use or the use of specified persons only, such as preliminary proxy material filed pursuant to Rule 14a-6 under the Securities Exchange Act."

The preliminary material is thus kept confidential. If it were not, particularly in the context of a proxy contest, it would be picked up by the newspapers and such publication itself would constitute a solicitation. In non-contest cases, confidentiality is frequently necessary because transactions contemplated are of a tentative nature and are still in the planning stage, or to prevent premature disclosure of information which in order to be fairly used should be communicated directly to all shareholders simultaneously in the form of final proxy material cleared by the Commission.

(3) Intra-Agency Memoranda.

While it is always desirable for public servants to work in a fishbowl to the greatest extent possible, there are

limitations. The statute recognizes these limitations in exempting in Subsection (e)(5) intra-agency memoranda or letters which would not be available to a private party in litigation with the agency. In explaining this exemption the House Report stated:

> Agency witnesses argue that a full and frank exchange of opinions would be impossible if all internal communications were made public. They contended, and with merit, that advice from staff assistants and the exchange of ideas among agency personnel would not be completely frank if they were forced to "operate in a fishbowl." Moreover, a Government agency cannot always operate effectively if it is required to disclose documents or information which it has received or generaged before it completes the process of regulation. This clause is intended to exempt from disclosure this and other information and records wherever necessary without, at the same time, permitting indiscriminate administrative secrecy.

Now, I certainly agree with that; and the Commission's Rule exempts such "intra-agency memoranda or letters ... ."

The need for preserving free channels of communication among members of the Commission and members of its staff impressed itself upon me recently in connection with the registration of a proposed securities offering. The matter was before the Commission upon a request that the registration be declared effective. The registration involved an offering of bonds in which a certain portion of the offering was to be sold pursuant to "delayed delivery contracts" to institutional purchasers. Such contracts are firm agreements to take down the bonds some period of time following the closing on the public offering. Of course, it such delayed delivery has a material effect upon the use of the proceeds from the sale of the securities or may entail interim financing, consideration should be given to appropriate disclosures. It developed that there was no need for such disclosures with respect to the particular offering, but I continued to be concerned about the disclosures which might be made in similar cases. The staff was engaged at that time, as it is presently, in a re-examination and supplementation of its guidelines for the examination of registration statements (to which I referred earlier) preparatory to publication of these materials for the guidance of the public. In a memorandum to the staff members working on this project, I suggested that they consider the

advisability of including a paragraph concerning the nature of disclosure deemed necessary in offerings of this type. In the course of the consideration of my suggestion, a tentative draft of a guideline was prepared and discussed. Upon consideration, the staff advised me of their opinion, in which I concurred, that publication of guideline in this area would be premature until more experience was acquired with the type of offering in question. They proposed instead to distribute a memorandum to members of the staff directing their attention to the point of concern and instructing them to consider what disclosures might be necessary in connection to future registration.

This type of exploratory communication between the Commission and its staff and among members of its staff is indispensable to the effective handling of the many questions which arise in the Commission's administration of the securities laws. Had any participant in this discussion been concerned that his memoranda, drafts, or other papers would be subject to public inspection, positions would have been polarized and the consideration would have been lengthened and would have suffered from a decrease in candor. Moreover, the memorandum distributed to the staff calling its attention to a possible problem area might never have been written. It can easily be seen that an accumulation of such impediments could slow the administrative process to a snail's pace.

(4) Fees.

As a last point, I would like to discuss briefly the provisions which the Commission's Rules make for payment of fees. The statute in Subsection (c) refers to published rules stating the, and I quote, "fees to the extent authorized by statute" in connection with requests for identifiable records. Authority to charge for services in connection with making such record available stems from the so-called User Charges Statute, 5 U.S.C. 140 (1946 ed). The Commission determined in its rules not to charge for services rendered during the first one-half man-hour. Thereafter, we have provided for a charge of $2.50 for each additional one-half man-hour. Since attorneys and other higher-paid personnel may be involved in this work, it may be that our charge is too low. However, we are waiting to see what our experience is before making revisions.

One problem which occurred to us in drafting our rules was that many of our files contain both public and non-public material and that a member of the public might well request the entire file as an identifiable record. It was determined, and I believe

properly, that in making the public portion of such a file available we should charge for our services in culling out the non-public records. We, accordingly, specifically provided in our rules as follows:

> Certain Commission records, such as correspondence to and from the Commission, are maintained in files which also contain non-public materials such as intra-agency and inter-agency memoranda and letters. If undue delay and expense is to be avoided, any person who wishes to examine such a record or to obtain a copy thereof should identify the letter or other similarly-filed record with particular specificity.

Another problem we anticipated was that caused by a request for numerous records which would entail the expenditure of considerable periods of time to locate. We did not believe that such a request should be permitted to monopolize the time of our limited staff to the detriment of other persons who might also be requesting records. We therefore reserved the right in our rules in such a situation to make equitable allocations of the time of our personnel to all persons requesting records.

* * *

Conclusion

In conclusion, I would like to reiterate that just as full disclosure, as embodied in the securities acts, is, I believe, good for the American securities markets, just so do I think full disclosure, as embodied in the Public Information Act, will be good for Government. The Public Information Act by its disclosure requirements should serve to insist that exercise of administrative discretion be on a rational and objective basis. This is to the good of all of us. It is an important statute, that seeks to balance the need for public knowledge of official actions with the need for public confidence in the confidentiality of its communications, where appropriate, with the Government. The impact of the Act has to be balanced. The benefits of administrative flexibility in dealing with changing conditions should not and need not be sacrificed to an administrative rigidity that would necessarily accompany indiscriminate publication of information supplied to an agency.

The attention to this statute and its implications by lawyers such as you is necessary to make it serve its purpose, and I applaud the attention you are giving it by your presence here today.

Thank you.