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Better Disclosure for Better Decisions®

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Via email: rule-comments@sec.gov

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

RE: Proposal to Publicly Release Staff Comment Letters and Non-Confidential Response Letters (File No. S7-28-04)

Dear Mr. Katz:

On June 24, 2004, via Press Release No. 2004-89, the Securities and Exchange Commission (SEC) announced its plan to begin making the comment letters issued by the Divisions of Corporation Finance and Investment Management on public filings, as well as non-confidential response letters, publicly available through its EDGAR database. This letter is respectfully submitted in response to a call for input regarding that proposal.

SEC Insight, Inc. pioneered the acquisition and analysis of SEC Division of Corporation Finance comment letters as an investment research tool starting in 2000. As a privately-held and independent investment research firm, we have analyzed literally thousands of pages of SEC comment letters and responses over the past few years – we believe more than anyone on Wall Street. This affords us a unique perspective regarding the impact certain aspects of the SEC's proposal may have on capital market participants.

We applaud Chairman Donaldson, the Commissioners, and Staff for this welcome initiative and anticipate its overall impact will be positive. We believe it represents one of the most meaningful increases in public company disclosure since corporate filings first became widely available to investors on EDGAR. It is for this reason that we call for its implementation with the utmost of transparency, diligence, and care for the interests of all involved. The balance of this letter speaks to the following:

1. The Investor's Perspective on Comment Letters;
2. Concerns Regarding the Rule-Making Process Employed Here;
3. SEC Insight's Specific Suggestions Regarding the Proposal; and
4. Closing Thoughts on the Proposal.

1. The Investor's Perspective on Comment Letters.

SEC comment letters, and their responses, are analytically rich. We consistently find them to be an important and helpful supplement to some of the more formal disclosure and communication mechanisms available to, and employed by, registrants. Currently, we still have to file individual Freedom of Information Act ("FOIA") requests to get them. Since Enron, the number of FOIA requests for SEC comment letters has risen sharply.

Like us, public companies know that SEC comment letters reveal areas of Staff concern about their accounting and/or disclosure practices. To the average securities analyst or investor, the SEC Staff is in the enviable position of being able to ask, and often secure the answers to, questions that are frequently dodged, dismissed, or ignored by a registrant when asked by a non-regulator. One of the best aspects of the SEC's proposal is that it will afford all investors inexpensive and easy access to this material without the need to file a FOIA request.

We have long believed that the majority of public companies chronically, and often deliberately, mislead investors regarding SEC matters. This is done through repeated failures to provide adequate and substantive disclosures regarding the same. The comment letter proposal provides one important means for investors to level the playing field with registrants by enhancing their ability to do what investors do best in transparent markets; that is, assess and discount risk.

For now, it remains that most investors – at all levels – have never seen an SEC comment letter, though many have heard of them. This is because, in the main, it remains unusual for a public company to disclose the existence, let alone the actual content, of an SEC comment letter. We see similar disclosure patterns displayed by registrants involved in SEC investigations as well.

While securities laws may compel a registrant to disclose a material event, it remains up to the registrant to determine materiality. In this context, when disclosures of an SEC comment letter or probe are actually made, they tend to be minimalist and primarily aimed at satisfying a legal requirement to disclose the existence of a material event. The substantive facts related to that same event, which investors require in order to make informed decisions, are often missing. It's as if the act of disclosure itself is telling you the matter is material, but the words accompanying it are designed to suggest otherwise, if they tell anything at all.

To illustrate, a common practice we've observed among registrants is to either not disclose an SEC inquiry or to do so well after the probe has commenced. We have seen disclosures pertaining to the receipt of comment letter correspondence crafted to appear as if only one comment letter was received by the registrant when, in fact, letters had been exchanged with the SEC for many months prior to the actual disclosure. In both cases, registrants may also highlight one or two minor-sounding issues from the probe or review, when the reality is that the challenges before the

registrant are potentially material. The typical disclosure pattern is that the registrant will make boiler plate disclosures, while failing or even refusing to provide substantive details, all the while pledging full cooperation with the SEC.

The release of comment letters will enhance capital market transparency if only for the fact they will neutralize registrants' proclivity to exploit investor lack of data or their ignorance regarding SEC process and procedure. Thus, the mass release of comment letters represents a dramatic shift in paradigm. As a result, this proposal is sure to have profound and lasting impacts on capital markets.

2. Concerns Regarding the Rule-Making Process Employed Here.

The comment letter proposal was announced through what amounts to a technically-dense press release: A medium that most investors didn't see but public companies and their advocates were not likely to miss. This is a departure from the traditional and well-established processes used by the SEC to seek comments from the public on new proposals and/or rule-making. This approach raises the concern that investors lack the awareness needed to become meaningfully engaged in the successful implementation of this proposal.

As we have seen in the past regarding proposals or rule-making before the agency, we encourage the SEC to seek the greatest number of public viewpoints possible on this comment letter proposal, particularly given its magnitude. We are concerned that the use of a press release to solicit comments, rather than the posting of an actual proposal on the SEC's web site as is customary, precludes this.

To illustrate, the SEC's proposal regarding Security Holder Director Nominations (*Release No.:* IC-26206; *File No.:* S7-19-03), was posted through the SEC's traditional rule-making process which resulted in well over 10,000 comments from a wide range of interested parties. As of today, fully three months after it was announced in June, the comment letter proposal has only received approximately one dozen letters. The longest of those letters are from well-financed public company advocates arguing for what, in our opinion, amounts to a weakening of the proposal.

Capital market participants clearly need to be given a more reasonable opportunity to become engaged in the process than what we've seen thus far. We respectfully suggest the SEC consider holding off on implementation of this proposal to allow for its immediate re-issue through normal and customary SEC channels. We believe the trade-off from potentially delaying this proposal is substantially out-weighed by the benefits to be gained from the many views market participants will surely have on the matter.

3. SEC Insight's Specific Suggestions Regarding the Proposal.

We respectfully offer the following suggestions on how to make certain the release of comment letters is as consistent and transparent as possible. Once complete, we believe it will be key that the SEC make certain that its final rules, procedures, and timetables regarding this proposal are as widely disseminated as possible.

- A. As an overriding guideline, we suggest that the release of comment letters should be as consistent as possible with what is currently permissible and

- required under the FOIA. For example, under the FOIA, comment letters are releasable as soon as a review is complete. This proposal needs to keep to that same standard. At a minimum, this means elimination of the proposed 45-day waiting period after a review ends. The 45-day waiting period is arbitrary and appears designed to serve the interest of registrants more than investors.
- B. There is no reason to provide public companies with advance notice that the Commission is planning to post their comment letters. Public companies already have these letters and can typically gauge the status of the review. Registrants have always been free to make their own disclosures regarding comment letters as they see fit and there is nothing in the proposal that would change that. As it stands today, comment letters are generally releasable under the FOIA without any advance notice to the registrant. Providing advance notice to registrants of the pending release of their comment letters would likely create an undue and costly administrative burden on the SEC with no discernable benefit to be had for investors.
- C. One of the reasons we believe the Commission has come forth with this proposal has to do with the exponential increase in FOIA requests received over the past few years.¹ While the goal of this proposal may be to grant easier access to comment letter records, one of the end-results would also likely be a meaningful reduction in the filing of FOIA requests. Yet, we are concerned that the need to submit FOIA requests will actually increase if this proposal is not implemented in a transparent and consistent manner. Specifically, I speak to those cases where records are withheld by Staff, for whatever reason, or reviews were conducted but the issuance of a comment letter was not deemed necessary.

In the past we have had reason to question whether documents we sought under the FOIA that were related to subjectively “sensitive” reviews were being unduly delayed or completely withheld from release. For this initiative to succeed, it will be essential that such “discretion” by Staff, to the extent it exists, be neither encouraged nor permitted.

Additionally, it’s also possible that under this proposal comment letters exchanged with a company involved in a Division of Enforcement matter could be held from release. However, these same documents may be releasable under the FOIA. This proposal needs to stick to this standard. Failing consistent release of comment letters, particularly in these sorts of circumstances, we fear a misguided “no news is good news” paradigm could emerge with investors inadvertently getting hurt in the process. This is especially true since the SEC doesn’t find the need to send comment letters to many of the companies it reviews.

- D. As with all comment letters, we advocate that the Commission consider releasing comment letters related to an acquisition and/or merger filing immediately upon completion of the review. When investors are asked by a management or board to approve a material transaction of any kind, it is empty and potentially self-

¹ Source: Securities and Exchange FOIA Annual Reports, 2000-2004.

serving for public company advocates to argue those same investors should be denied as much information as possible in order to make an informed decision.

Rapid release of comment letters in these instances enhances the information available to that very group with the most to lose in such scenarios – the shareholders.

- E. The blanket proposal requiring all registrants to submit so-called Tandy language in their response letters will keep the investing public from knowing of those instances where the registrant may be involved in a matter involving the Division of Enforcement. The universal use of Tandy language by registrants will remove a potentially valuable piece of data from investors. This piece of the proposal, perhaps inadvertently, puts the SEC in the position of becoming complicit in helping registrants keep potentially material information from investors and should be reconsidered by Staff. There is no shortage of registrants keeping material information from investors.
- F. We suggest additional language be required of all registrants in their responses to any SEC comment letter and their public disclosures regarding the same.

Specifically, we ask that all registrants be required to acknowledge that they recognize an SEC review is not comprehensive, nor is it designed to be. We too often hear companies and their supporters overstate the outcome of SEC review or investigative activity. This is most commonly done by implying that the completion and/or termination of the same bestows some sort of “blessing” or “approval” by the SEC, or that the SEC went through a registrant’s filings, “with a fine tooth comb,” when none of the above are true.

Compelling registrants to openly acknowledge the limitations inherent in any review process will go far in neutralizing any undue or unintended implications that could arise. SEC-initiated efforts to educate investors regarding the same will also help.

- G. Comment letters exchanged in those instances where a registration was withdrawn by a privately held company which was considering public markets for the first time should not be released. In the event, however, that the same company later does become public, then all comment letters generated should be released once the reviews are completed.

However, in those instances where the registration is withdrawn by a registrant that already has securities – of any kind – available and trading on public markets, the comment letters should be released, regardless of why the registration was withdrawn. Not only is this consistent with the FOIA, we have also seen instances where a registration is withdrawn because of Staff objections that the registrant either cannot or will not resolve in a timely manner. Rather than remedy them, the public company will withdraw the registration and not inform investors of the deficiencies noted by Staff. Investors ultimately lose in these scenarios.

- H. Comment letter correspondence exchanged with foreign-based registrants should not be given any different or preferential treatment than those exchanged with US-domiciled registrants. If anything, the standards should be higher as investors are already challenged with trying to obtain adequate information on foreign-based companies.
- I. In those instances of extended reviews, perhaps those lasting more than a few months, consideration should be given to releasing comment letters prior to the conclusion of the review. Often in the case of an extended review, the damage to investors is done before an extended review is finished and they have any chance to even know there was a problem. It is not hard to imagine scenarios where registrants might find it beneficial to drag-out a review to delay the release of comment letters. Without the pressure of imminent disclosure, there is nothing to keep this from happening. Implementation of some sort of a "hard-stop-release-certain-date" on comment letters gives registrants added incentive to cooperate more fully with the SEC.
- J. To the extent it does not create an undue burden, we ask that the SEC consider posting all comment letters in historical archives as well. Our experience is that it is analytically meaningful to have access to comment letters going back a period of at least three years. Perhaps the SEC could consider posting all comment letters and their responses initiated in Fiscal years 2001, 2002, and 2003.
- K. This point speaks to the issue of confidential information. We fully expect confidentiality assertions to dramatically increase once comment letters start to be posted. In our experience in using the FOIA, however, we've observed that registrants frequently make what we would characterize as specious assertions of confidentiality.

The mechanisms presently available to the SEC FOIA requester seeking to challenge a confidentiality assertion are burdensome and time consuming. We've also observed inconsistencies by Staff in terms of following-up on and processing them in a timely and consistent manner. The challenges in processing confidentiality assertions is a reality that one should assume will become increasingly known to and exploited by registrants going forward. Presently, and even with the FOIA, one cannot even get a copy of the guidelines used by Staff when considering confidentiality challenges.

We suggest the SEC needs to promulgate new and consistent rules and procedures regarding the release of confidential information. Failing this, and at a minimum, transparency and predictability regarding how confidentiality assertions will be evaluated and decided upon needs to be meaningfully increased from present levels. Both investors and registrants need to have confidence that confidentiality assertions and challenges thereto will be handled in as fair, consistent, and rapid a manner as possible.

We also advocate that the current practice of the Division of Corporation Finance regarding confidentiality assertions related to registrations stay as it is; that is,

issues related to confidential treatment requests need to be resolved prior to the effectiveness of any registration a registrant has pending at the time.

In addition to this, we suggest that all confidentiality assertions made by registrants be required to be resolved between the registrant and the Commission as one of the requirements of ending any review. Not only will this potentially limit specious confidentiality assertions by registrants, it will likely contribute to avoiding the potential cost and litigation that could come from challenges to them later.

- L. In the face of knowing that their comment letters are going to be released, we expect some registrants will seek to have as many items as possible pertaining to their reviews “off the record”, as would be the case in a verbal, as opposed, to written exchange. We call upon Staff to actively discourage these overtures.
- M. Finally, we ask that Staff implement a mechanism to enable the investing public to appropriately give suggestions, submit requests, and ideas regarding issues they would like to see brought up in a review. To illustrate, in the past we have seen registrants routinely argue in their response letters

that investors are not interested in certain disclosures proposed by Staff when, in fact, they are. But there currently appears no means for Staff to know the investors’ point-of-view beyond the submission of a complaint or tip about a registrant to the Division of Enforcement.² Analysts and investors who follow companies closely are in touch with the market’s sensitivities to the financial nuances and disclosure shortcomings of a registrant. By opening an alternative channel of communication to Staff from investors, even if only one-way, investor perspectives will be better known which will likely enhance the outcome of reviews.

4. Closing Thoughts on the Proposal.

The promise of easy access to SEC comment letters is one important victory for open markets and investors. We again applaud Chairman Donaldson and the SEC for this proposal.

While we would like this proposal to be implemented as swiftly and smoothly as possible, we also understand the gravity of the issues involved here and the likely impact they will have on market participants. Given this, we feel that the mission of the SEC to serve as the investor’s advocate suggests there is more the agency can and should do to make sure this proposal happens in a way that truly benefits and protects investors.

On behalf of SEC Insight, Inc., I thank you for the opportunity to present our observations and suggestions regarding the comment letter proposal. I am pleased to make myself available to Staff if there is any way I can be of further assistance.

² Source: Securities and Exchange Commission web site at www.sec.gov.

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Sincerely,

/s/ John P. Gavin

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