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January 28, 2005

Chairman William H. Donaldson
U.S. Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549

Dear Chairman Donaldson:

I previously sent a general letter to the SEC on securities offering reform which predated, by almost a month, the publication of proposed SEC Securities Offering Reform, Release 33-8501; File No. S7-38-04. I am now writing to expressly comment on the published proposed rule.

I believe the SEC is taking a major step forward in recognizing the fact that the world has changed since the Acts of 1933 and 1934 (hereafter the Acts). Prior to the Acts, issuing firms regularly failed to issue financial statements resulting in an inability for investors to make informed judgments on the worth of an IPO. In addition firms faced little legal liability with regard to the failure to disclose information prior to the offering. The Acts changed that as illustrated in a paper by Seha Tinic.[1] As part of his study, Professor Tinic examines the number of civil suits and SEC proceedings for securities offerings over the period 1915-1986. From 1915 until 1934 there were ***no*** actions. From 1935 through 1986 there were 305. Of those 75% were won by plaintiffs. Professor Tinic goes on to hypothesize that stock issues are underpriced to provide a form of insurance to issuing firms that may be sued due to the failure to disclose information.

The implications of Professor Tinic's paper are clear. The Acts have provided a very strong motive for issuing firms to disclose all relevant information about an offering in the prospectus and to not deviate from what is in the prospectus. There is now a long history of

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[1] See Seha M. Tinic, "Anatomy of Initial Public Offerings of Common Stock" *Journal of Finance*, September, 1988, pp. 789-822.

issuing firms being sued by investors. This is a very strong deterrent. Therefore the previous restrictions on the written prospectus being the almost exclusive source of information are no longer necessary.

The Acts and subsequent amendments created Self Regulating Organizations and charged them with policing their members and listed firms. This provides a deterrent to those firms that represent, trade, or professionally research issuing companies. For example, earlier this month NASD fined an analyst $75,000 for circulating false rumors about RF Micro Devices. So Issuing firms are not the only entities now facing legal liability for making mis-statements.

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rior to the Acts, media coverage of security offerings was hampered by poor means of communication and expensive travel costs. Today, the media can easily research and report on virtually any company in the world with the only barrier being language. The media have become, as the SEC acknowledges in the proposed rule, an important investment tool.

The proposal by the SEC to create free-writing prospectuses recognizes the existing legal and information environment. I feel that investors will be well served if issuers are allowed to speak with unaffiliated and uncompensated media during the offering process. If the media outlet is compensated for publishing information about the company then that communication should clearly state the compensation arrangement. In other words investors need to be able to differentiate between an infomercial and a news story.

Given the wide-spread use of electronically readable prospectuses on file with the SEC, it is my feeling that the SEC does not need to require unseasoned issuers to deliver a copy of the formal prospectus before they speak with unaffiliated and uncompensated media. Given the rash of media embarrassments of late, reporters are likely to check and double check the facts in any story they write. Reporters are making extensive use of SEC filings on the Edgar database. Having documents on file there should be sufficient for issuing firms. A formal delivery process only increases the costs of an offering. This disadvantages smaller firms who I think stand to gain the most from this rule.

Previously, the SEC has designed registration processes that reduced filing requirements for small firms. [2] These rules allow issuing firms to go public without using an investment bank – a so-called Direct Public Offering (DPO). As I pointed out in my first letter to the SEC on offering reform, most DPOs fail. .Although the internet has lowered the cost of delivering documents to potential investors of an offering, most firms lack a list of potential investors and rely on the better mousetrap theory to gain investors. As with the proverbial better mouse trap, the world does not beat a path to the doors of these firms. What they need is a way to let people know about the documents on their web sites. This can be done through the media.

Therefore, allowing these small firms to talk with the media without fear of violating quiet period rules would increase the chances of successful offerings. This would be consistent with the position of the SEC to help small offerings be successful. Without a relaxation in the rules governing communications with the media for small unseasoned issuing firms, SEC rules governing offerings of less than $5,000,000 are useless and should be repealed.

The same rules governing communications with the media also stifle innovation in investment banking – by favoring established firms with long client lists. An investment banking firm with an innovative idea cannot capitalize on it unless they have a large list of clients to sell issues to through the normal offering process.[3] A good case in point is a firm that I have served as an advisor to – Civilian Capital. That firm sought to securitize film productions but was severely hampered by the lack of an established client list. The amounts of capital sought by the firms Civilian represents are too small for most existing investment banks (under $10 million).

[2] In particular: the Small Corporate Offering Registration and Schedule A offerings.

[3] During the cooling off period, it is common for investment banking firms to obtain indications from their customers as to their interest in an issue – essentially pre-selling it before the issue becomes effective.

Therefore, their ideas are not attractive to existing investment banks – but are very attractive to the film industry.

However, existing rules have prevented Civilian from contacting the media to drive potential investors to their web site (and their filings on the SEC's Edgar database). If they were allowed to communicate more easily with the media, the chances of their success (like those of other small offerings) would be greatly increased. When dealing with secondary markets, the SEC always touts the value of competition and innovation. Yet in the area of primary offerings, they have heretofore stifled it. The rules governing communications of issuing firms (and their representatives) with the media should be loosened and no prospectus delivery requirement should be imposed on communications with unaffiliated and uncompensated media.

Thank you for your consideration of my letter in this matter.

Sincerely;

Daniel G. Weaver, Ph.D.
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Associate Director, Whitcomb Center for Research in Financial Services