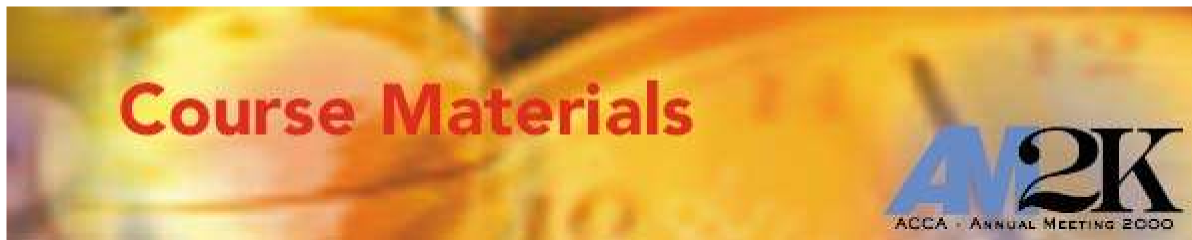


DELIVERING STRATEGIC SOLUTIONS ACCA'S 2000 ANNUAL MEETING

April 27, 2000

Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street N.W.
Washington, DC 20459
E-mail address: rule-comments@sec.gov

Re: Proposed Selective Disclosure and Insider Trading Rules; File No. S7-31-99

Dear Mr. Katz:

The Corporate and Securities Law Committee of the American Corporate Counsel Association ("ACCA") is pleased to participate in this important rulemaking proceeding. ACCA is a national bar association exclusively for in-house corporate counsel. ACCA has more than 11,000 individual members who act as in-house counsel to more than 4,400 business entities. The Corporate and Securities Law Committee is the largest of ACCA's national committees and includes in its membership attorneys from hundreds of corporations subject to SEC disclosure requirements. Corporate counsel play a pivotal role in the corporate disclosure process. Our members appreciate that public companies have a responsibility to provide full and fair disclosure of material information as required by legal and self-regulatory standards.

We continue to support the Commission's efforts to reform selective disclosure practices. Selective disclosure disserves public companies, their shareholders and all investors. It gives an unfair advantage to a select group of market participants, which undermines public perceptions about the fairness of the U.S. securities markets. While the extent of abuse of selectively disclosed information may be difficult to measure precisely, we believe that rulemaking initiatives by the Commission and stepped up enforcement activity can lead to improved corporate disclosure practices.

In our view, proposed Regulation FD, if adopted, should not be used to regulate and sanction corporate efforts made in good faith to fairly disclose information. We believe that adoption of a revised form of Regulation FD may reduce the extent, or at least the perception, of selective disclosure. However, we have significant concerns related to the breadth of the proposed regulation. Our comments and suggestions address important areas where we believe the proposed regulation must change to be more targeted, balanced and fair — and ultimately, to achieve the Commission's objectives without imposing undue and insuperable burdens on corporate issuers.

Selective Disclosure "to any other person outside the issuer"

Regulation FD is proposed to apply to any communication about the company or its securities "to any person

or persons outside the issuer . . . " We are concerned that such broad language could require corporate counsel to devise a means to monitor virtually all external corporate communications, including those with vendors, customers and other businesses. Interaction between corporate personnel and these categories of persons does not entail any meaningful risk of the type of selective disclosure to analysts and institutional investors that is difficult to address given the U.S. Supreme Court's decision in Dirks v. SEC. Existing insider trading law together with the new proposed insider trading rules (i.e., Rules 10b5-1 and 10b5-2) should be sufficient to assure legal compliance by these types of recipients of corporate information. Therefore, we urge the Commission to limit the scope of Regulation FD to communications to analysts, institutional investors and other market professionals, which are the types of persons outside a company that pose the biggest risk with respect to receiving and taking unfair advantage of selectively disclosed information.

Disclosures by "a person acting on behalf of an issuer"

We also urge the Commission to refine the definition of "person acting on behalf of an issuer." Today, virtually all major public companies have elaborate internal compliance systems intended to protect confidential corporate information, manage the process of external communication and prevent the misuse of confidential information by insiders and others. A key element of the efficacy of these existing systems is the ability to clearly identify the specific persons within the company who are subject to particular restraints and procedures. By contrast, the proposed definition of corporate personnel within the ambit of Regulation FD seems unduly vague and imprecise. For example, it could include literally any employee of the issuer who communicates in the course of "acting within the scope of his or her authority" even if the person does not have authority to make the kind of communication, such as to analysts and institutional investors, that may result in a disclosure that would be problematic under Regulation FD. Similarly, the term "agent" could be construed to include a broad range of non-employees who currently are not, and should not have to be, included within the scope of internal corporate compliance systems. While we appreciate the Commission's acknowledgement that disclosures by persons acting outside the scope of their authority would not be deemed to be a person acting on behalf of the issuer, the exception would not address many other situations such as an innocent disclosure of material information in the course of business dealings between an employee and an outside party. Nor do we think it is realistic to require confidentiality agreements from the raft of outside parties that participate in routine business discussions.

Instead, we think the term "person acting on behalf of the issuer" should be more clearly defined in a manner that focuses on the types of employees and agents involved in communications with market professionals. We suggest the Commission consider a much narrower definition, such as directors, executive officers and "any other person with specific authority to communicate on behalf of the issuer to analysts, institutional investors and other market professionals with respect to financial matters." This kind of revision would be in line with the Commission's suggestion in the proposing release that issuers designate a limited number of persons who are authorized to make market-sensitive disclosures.

We also believe that persons ultimately covered by the regulation who act on behalf of the issuer should be allowed to presume confidentiality when information is given under circumstances in which the person reasonably believes there is a duty of confidentiality or advises the recipient of the confidential nature of the communication and has no reason to believe it will be misused. It is unrealistic to assume corporate officials will be able to negotiate written confidentiality agreements in every relevant context to protect against selective disclosures. To the extent a person representing the issuer reasonably believes information is released to a third party for a legitimate business purpose and will not be selectively disclosed, such persons and the issuers they represent should not be responsible for a breach of trust by the recipients of the information.

Timing of required public disclosures

Proposed Regulation FD makes a distinction between intentional and non-intentional selective disclosures.

For intentional disclosures of material information, the regulation would require simultaneous public disclosure of the information. If there has been a non-intentional disclosure, then the issuer would be required to make public disclosure promptly in accordance with the regulation. In general, we believe that this is a logical way to distinguish the timing of disclosures for purposes of the regulation.

Intentional Selective Disclosures

Under the proposed regulation a selective disclosure of material information would be intentional if an individual who made a disclosure knew, or was reckless in not knowing, material nonpublic information was being communicated. We are extremely concerned with this aspect of the proposal that would incorporate "recklessness" into the definition of "intentional." We believe it should be sufficient to utilize an actual knowledge test for purposes of triggering a disclosure obligation under the regulation, which seeks to prevent abusive selective disclosure practices. Recklessness as a legal concept has not offered clear guidance to corporations seeking to comply with prescribed standards of conduct. Professor Robert Prentice has observed that,

> . . . categories of conduct lie on a continuum running from simple negligence to gross negligence to recklessness and finally to scienter. Distinguishing fine lines of demarcation is nearly impossible. Rather, these concepts bleed into one another in a confusing fashion.

Even the definition of recklessness laid out by the court in Sundstrand Corp. v. Sun Chemical Corp., 553 F. 2d 1033, 1045 (7th Cir.), cert. denied, 434 U.S. 875 (1977), "can cause confusion" according to a respected commentator.

Moreover, including a recklessness standard as a disclosure trigger will greatly heighten corporate concerns about the extent to which the Commission staff may launch enforcement actions targeted at issuers under Regulation FD. Issuers are already very uneasy about the renewed focus on the internal process by which corporations make judgments about the materiality of information, which often take place in compressed timeframes and without the assistance of counsel. The difficulties in such judgments are compounded by the directive under SAB 99 to carefully consider qualitative information. With the benefit of hindsight, honest errors in judgment may be viewed in a more extreme light by members of the Commission's enforcement staff. A natural reaction by corporate managers to such concerns could be to curtail or eliminate conferences and other communications with analysts. But even putting aside such potential chilling effect, it is quite clear that such a gray recklessness standard will result in demands for counsel's input on virtually all materiality judgments. This will impose an enormous and unjustifiable strain on corporate compliance systems, which already allocate significant legal resources and time to "materiality calls" and similar types of disclosure issues.

If the Commission insists on including recklessness as an element of the definition of intentional, then it would be imperative to add a safeharbor or other clear statement to the effect that good faith attempts to comply with the regulation, whether involving judgments about materiality, beliefs about the public nature of information or otherwise, shall not be deemed to be reckless under the regulation. As we previously stated, we believe the regulation should be designed to sanction clear attempts to selectively disclose material information, and in so doing, will result in improving deficient procedures where necessary. The proposed regulation should not be used to penalize companies and corporate officials who try to "do the right thing" by following reasonable procedures that contemplate and reinforce proper disclosure practices. We note that many of the procedures recommended in the Release, such as limiting the corporate officials authorized to talk to analysts, recording analyst discussions and not answering questions where officials are unsure of the materiality of the response, are already practices followed in some manner by many public companies.

We also note that in triggering a disclosure obligation, the proposed regulation would have the unintended effect of compromising a company's "no comment" posture and ability to keep material information

non-disclosed for legitimate business reasons. This would be most egregious and unfair to public companies in situations where potentially material information is unintentionally (and possibly "recklessly") disclosed in a private context and subsequently discovered by a "senior official," thereby triggering a disclosure obligation, even though the information may never reach the public market. Given the importance to issuers of timing the public disclosure of material corporate developments, essentially creating a new affirmative disclosure obligation in many of these types of situations that do not involve intentional conduct would be a significant deviation from current law, competitively harmful to public companies and unreasonably intrusive. Again, a safeharbor or other clarifying statement relating to good faith conduct would mitigate the potential impact of these situations.

Non-intentional Selective Disclosures

Our comments and suggestions above relating to "recklessness" are equally applicable to the part of Regulation FD which provides that a non-intentional selective disclosure would be a breach of the regulation if not "promptly" disclosed to the public within 24 hours of a senior official knowing, or being "reckless" in not knowing, of the selective disclosure. Again, we believe in-house counsel must be given some comfort that good faith attempts to not selectively disclose material information, including difficult judgments made about "materiality" that prove to be wrong in hindsight, will not subject a company or its officials to a violation of Regulation FD. Otherwise, there will be enormous pressure to overlawyer all corporate disclosures, which would be an unjustifiable and extremely onerous practice.

We also believe the timing requirement relating to non-intentional disclosures should not be a 24 hour period, because one could easily foresee circumstances where it would be difficult to organize the necessary internal and external resources, gather all the relevant facts and prepare a proper public disclosure document within that time frame. We suggest the timing standard should be "as soon as reasonably practicable" or merely "promptly," which standard would imply disclosure even before 24 hours elapses if reasonable under the circumstances. We also note that under the proposed regulation, it is very difficult to determine when the disclosure period would start to run in the case of non-intentional disclosures subsequently discovered.

We also suggest that the trigger mechanism for non-intentional disclosures under the proposed regulation would be more appropriate if the definition of "senior official" was not so broad to include "any investor relations or public relations officer or any person with similar functions." It may make sense to include within the definition the chief investor relations officer and the chief public relations officer. Large public companies, however, can have dozens of employees with some responsibility associated with public relations or corporate communications. Employees with responsibility for external communications unrelated to the investment community, other than the head of corporate communications, should not be deemed a senior official because these persons are not likely to be in a position or have the appropriate sensitivities to become aware of non-intentional selective disclosures under Regulation FD. Attempting to construct an internal compliance system to include such persons would be needlessly burdensome to issuers while adding little if anything to compliance. We also believe directors should not be included in the definition of senior official. They are typically not involved in many communications to the financial community and are not well positioned to identify unintended selectively disclosed information.

The reference to "any person performing similar functions" in the proposed definition of senior official also introduces another element of uncertainty. For example, would a business officer who occasionally performs a PR responsibility fit within the definition? In sum, we believe the definition of "senior official" for purposes of unintentional disclosures should be based on either the individual's actual seniority within the organization or relevant functional responsibility to deal with the investment community since these are the types of persons that we think could reasonably be expected to detect and address non-intentional selective disclosures.

Public Disclosure and Corporate Websites

We do not believe the proposal should add a new Item 10 to Form 8-K for disclosures required by Regulation FD. This would not be preferable to using Item 5 of Form 8-K, because a new Item 10 could be used as an admission of materiality by the plaintiffs' bar to the detriment of an issuer in other contexts, eg, a fraud on the market suit for delayed disclosure. No doubt there will be many instances where corporations will err on the safe side and file an 8-K under Regulation FD, even though the materiality of the disclosure is unclear, and these filings should not be used to create unfair presumptions.

Regulation FD would consider as adequate public disclosure, in addition to the enumerated disclosure methods, "any other method of disclosure that is reasonably designed to provide broad public access to the information and does not exclude any members of the public from access." This is a flexible standard that will give issuers several different methods of dissemination. Among other things, there is a growing trend among companies to webcast analysts' meetings to the media and the public generally, and we believe this may be a common approach to minimizing the risk of violations of Regulation FD.

We disagree, however, with the Commission's apparent conclusion that posting information to a corporate website would not be a method reasonably designed to provide broad public access to information. A Harris survey conducted in December, 1999 reported that 69% of all U.S. adults now use computers and that 81% of all P.C. users go online. The survey found that the online population has increased six fold in four years to 56% of all adults or 115 million people. Thus information posted to websites is undoubtedly broadly accessible to the public in the same way that a press release issued to a wire service is available, or for that matter information that is available on Edgar.

The current data suggests a sea change from studies cited within the last couple of years that showed only 20% of U.S. households had Internet access and that search tools on the Internet were relatively immature. Given the continuing explosive growth in Internet use reflected in the Harris survey and the ease with which users can access corporate websites, there can be no doubt that the individual investors can at least as easily access information about public companies through the Internet as through the traditional print media. Most importantly, a broad base of investors knows about and frequently visits corporate websites. According to a recent member survey by the National Association of Investment Clubs, 75% of individual investors visit a company's website before making their investment.

We believe the Commission should reconsider the implication of footnote 51 of the Release that information on an issuer's website should not be deemed public until investors are alerted that information is available. A website posting is no different than issuance of a press release. In our view, the Internet has reached a level of accessibility, and enough investors know that timely corporate information can be found on an issuer's website, to support treating a corporate website as a satisfactory avenue for public disclosure. At the very least, the Release should acknowledge that a posting on a corporate website, and a broad notice alerting investors that the information has been so posted, should be deemed adequate public disclosure. This dissemination of information would be functionally equivalent to a webcast and broad public notice thereof, which is specifically supported in the Release as adequate public disclosure.

Liability Issues

It is helpful for the proposing release to state that no private liability will arise from a violation of Regulation FD. Nevertheless, we believe Regulation FD will increase the opportunities for "second-guessing" by private litigants of the nature and timing of disclosures. SEC enforcement action under Regulation FD obviously will also be of great concern to issuers.

We strongly believe, as noted above, that "recklessness" be eliminated as a standard for violation under the regulation, or that there be clarification of how that standard would be interpreted. As discussed above, we are most concerned about the difficulty counsel has in making judgments about materiality. Decisions must constantly be made by in-house counsel about whether numerous individual facts, opinions, speculations and

sound bites are — or could be deemed to be — "material" in the total mix of information available. Difficult but honest calls are often made to help analysts build their "mosaic" — not to provide a "material tip." Under Regulation FD, these types of materiality judgments will often be made in hindsight. If a corporation's stock price moves in the 24 hours following an inadvertent disclosure, a decision may be made to disclose; if it does not, the opposite may be made. Significantly, in neither case will any such judgment be dispositive of the materiality question. Given this type of slippery slope, liability for "reckless" conduct will be fraught with uncertainty both before and after the fact.

We also strongly believe that innocent or inadvertent violations of the regulation, such as good faith judgments about "materiality," should never deprive an issuer of access to "short form" registration statements or disqualify Rule 144 sales even if such conduct might be deemed "reckless." The unavailability of streamlined registration or the Rule 144 sales process could have significant adverse impacts on capital raising and the operation of employee benefit programs, and this draconian consequence should only apply, if at all, to deliberate and intentional violations of Regulation FD. Moreover, given the difficulty in identifying or defining reckless conduct, an issuer would never really know whether it properly qualified for use of a short form registration or whether sales were exempt under Rule 144. This clearly would be an unworkable situation.

We are also struck by the fact that Regulation FD places all of the burden of compliance and the attendant liability for non-compliance upon issuers, and does not address the analyst community in any meaningful way. The adopting release should make clear that Regulation FD is not intended in any way to give financial analysts and others free license to capitalize on valuable corporate information which they have reason to believe is not yet public, and that misuse of selectively disclosed information may result in Commission enforcement actions against analysts, possibly for aiding and abetting Regulation FD violations, among other actions. We urge the Commission's staff to redouble its efforts to scrutinize how investment banking firms safeguard the confidential corporate information they receive and to bring enforcement actions against those who misuse such information for personal or institutional benefit.

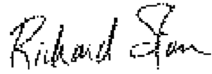
Proposed Rule 10b5-1 and Rule 10b5-2

In general we support the adoption of proposed Rules 10b5-1 and 10b5-2. We are concerned, however, with the definition of "on the basis of" in proposed Rule 10b5-1. The release carefully traces the judicial evolution of the "knowing possession" and "use" standards, and expresses a preference for the "knowing possession" standard. Proposed Rule 10b5-1, however, uses an "aware of" standard, which we find to be both different and potentially troubling. Under this standard, for example, a person could face liability if another party made him "aware of" the material information even though it did not register with him at a cognitive level. The knowledge element should be substituted because that is the recognized, longstanding basis for satisfying the intent element required by insider trading law.

* * *

In conclusion, we believe that revisions to Regulation FD, along the lines described in this comment letter, are necessary to ensure that the regulation is more targeted to achieve its objectives. We agree a regulation can be crafted to enhance fairer disclosure by issuers, or at least the perception of such fairness, and possibly diminish opportunities for market professionals and others to take unfair advantage of their access to important corporate information. However, the Commission should be very careful not to impose a new regulatory scheme that unduly and unfairly burdens issuers and their compliance systems and sanctions good faith attempts by responsible corporate citizens to provide full and fair disclosure.

Sincerely yours,



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