NEW YORK STATE BAR ASSOCIATION
Albany, New York

October 25, 1996

By Mail and Electronic Mail
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Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Stop 6-9
Washington, D.C. 20549

Re: Securities Act Concepts and Their Effects On Capital Formation (File #S7-19-96)

Ladies and Gentlemen:

The Committee on Securities Regulation of the Business Law Section of the New York State Bar Association appreciates the opportunity to comment on Release Nos. 33-7314 and 34-37480, dated July 25, 1996 (the "Concept Release"), in which the Securities and Exchange Commission (the "Commission") requests comments on a variety of concepts to reform the current regulation of the capital formation process under the Securities Act of 1933 (the "Securities Act").

The Committee on Securities Regulation (the "Committee") is composed of members of the New York Bar, a principal part of whose practice is in securities regulation. The Committee includes lawyers in private practice and in corporation law departments. A draft of this letter was circulated for comment among members of the Committee and the views expressed in this letter are generally consistent with those of the majority of the members who reviewed the letter in draft form. The views set forth in this letter, however, are those of the Committee and do not necessarily reflect the views of the organizations with which its members are associated, the New York State Bar Association, or its Business Law Section.

I. CONCEPTUAL OVERVIEW

We applaud the efforts of the Advisory Committee on the Capital Formation and Regulatory Processes (the "Advisory Committee") and, particularly, the efforts of Commissioner Stephen M. H. Wallman whose leadership and insight were instrumental in the publication of the Report of the Advisory Committee which he chaired, dated July 24, 1996 (the "Wallman Report"). The Wallman Report

reflects the unanimous recommendation of the Advisory Committee to both strengthen existing investor safeguards and reduce the costs of capital formation by establishing a company-based registration system ("Company Registration"). We support in concept the conclusions of the Advisory Committee contained in the Wallman Report and recommend the adoption by the Commission of the voluntary "pilot" program for seasoned issuers contemplated therein. We also concur in the separate statement (the "Separate Statement") of three members of the Advisory Committee contained in Section IV of the Wallman Report and we urge the Commission to consider the conclusions set forth in the Separate Statement in conjunction with action taken in response to the comments received with respect to the Concept Release.

We also commend the efforts of the Task Force on Disclosure Simplification as reflected in the Report of the Task Force, dated March 1996 (the "Task Force Report"). Many of the recommendations contained in the Task Force Report would streamline, simplify and modernize the regulation of capital formation without diminishing investor protection. We note that the Task Force Report is not limited to Securities Act proposals and that in many respects the recommendations of the Task Force are consistent with or duplicate those of the Wallman Report.

The Concept Release poses numerous specific questions to which the Commission seeks responses. Rather than raising strictly legal issues, a substantial number of these questions seek information concerning such matters as the efficiency of the trading markets, as to which our Committee is not necessarily equipped to respond. We further note that the Concept Release raises many questions that were considered by the Advisory Committee during the period of more than 16 months of its deliberations, for which it had resources not readily available to the securities practitioner. Therefore, as to conclusions of the Advisory Committee which do not appear to our Committee to be clearly "right" or "wrong", we are inclined to accept the recommendations of the Wallman Report as the right foundation for further development and analysis.

In view of the expansive nature of the Concept Release we have chosen to comment only on selected portions, including the identification of certain questions that we would initially answer by accepting the conclusions of the Wallman Report. However, we also believe that certain conclusions contained in the Wallman Report merit further examination and, as to those issues believed to be sufficiently important to warrant separate discussion, we have presented alternatives for possible consideration by the Commission.

Before setting forth our specific comments to the Concept Release, however, we wish to stress the fact that our Committee believes that the conceptual changes recommended by the Wallman Report and fully supported in most cases by the

Task Force Report should be adopted at this tune substantially as recommended by the Advisory Committee. Although the concept of Company Registration may be considered by some as an extreme step, we concur in the conclusion of the Advisory Committee that this model is the logical culmination of integrated disclosure and is well suited to a marketplace characterized by a relatively limited volume of securities offerings in the primary market and a far greater volume of secondary market trading in securities. The principal improvements to the current regulatory system that would result from Company Registration would include the following:

1. Speedier access to the market, including reduced transnational documentation; greater flexibility to go to the market more often in lesser amounts at lower transaction costs; and the elimination of SEC Staff review of Securities Act filings in most cases combined with enhanced review of Exchange Act filings and improved disclosure practices by issuers.

2. Payment of filing fees at the tune of sale rather than in advance.

3. Elimination of the market overhang and price distortions that may result from placing equity securities on a universal shelf.

4. Reduction in the time and expense devoted by the SEC Staff and securities practitioners to issues of gun-jumping, integration, general solicitation, restricted securities and other concepts developed to separate the public and private, domestic and offshore markets.

5. More flexibility in marketing efforts since the timing and content of the prospectus would be driven by the informational needs of investors, not compliance with technical rules.

6. Lower risk premiums paid on the cost of capital as a result of enhanced disclosure practices applicable to Exchange Act reporting of information incorporated by reference in Securities Act filings.

7. Elimination of the illiquidity discounts charged to issuers in sales of restricted securities combined with full liquidity for investors for what otherwise would be privately placed securities.

8. Elimination of the cost and delay inherent in registration requirements and resale restrictions with respect to most directors and officers that are imposed as a result of their status as "affiliates".

We agree with the Advisory Committee that the ultimate goal of Company Registration should be to extend the benefits of this system to virtually all public

companies that previously have conducted a public offering. We also recognize that an extension of the system to less seasoned companies may require disclosure safeguards or other modifications depending upon experience with the pilot program. We therefore support the conclusion of the Wallman Report that the system should be phased in gradually, beginning with larger, more seasoned companies of the type recommended by the Advisory Committee. In our view the pilot program should go forward to permit active experimentation.

We also note that the exemptive authority granted to the Commission under the recently enacted National Securities Markets Improvement Act of 1996, as supported by Chairman Arthur Levitt in his testimony before a Senate Committee, provides the Commission with the authority necessary to implement the proposals contained in the Wallman Report. (Testimony before the Committee on Banking, Housing and Urban Affairs, June 5, 1996, at page 18)

II. COMPANY REGISTRATION -- SPECIFIC COMMENTS

The following comments are designed solely to improve the Company Registration model recommended by the Advisory Committee. These suggestions should not be viewed as a precondition to our Committee's recommendation of the adoption of a pilot program. Rather, they are suggestions which we feel merit further examination and review by the Commission.

1. The Offering Process. We believe consideration should be given to raising the de minim is level for the required filing of a transactional Form 8-K from 3% to 5% of the issuer's public float. Our principal reasons for this suggestion are twofold. First, we believe it may help to avoid some of the resistance to the voluntary participation of certain issuers in the Company Registration system by further liberalizing the coverage of Section 11 liability. Second, we believe that the 5% standard has become customary in a number of other contexts and would further enhance the efforts toward simplification of the system, e.g., the threshold requirements for filing Schedules 13D/G and Schedule 14D. As noted in Section III.2(i) below, however, additional clarification with respect to the method of providing pricing information for an offering is recommended.

2. Prospectus Delivery. Since we believe that one of the principal objectives of Company Registration should be the simplification of the registration process, we are concerned that the prospectus delivery requirements outlined in the Wallman Report may be overly complicated by having at least three separate tiers. We would adopt the suggestion contained in the Wallman Report that the Commission seriously consider the elimination of the second tier (Non-routine Transactions) and extending the procedures for Routine Transactions to the second tier. Thus, traditional prospectus delivery would not be required for Non-

routine Transactions (as distinguished from Extraordinary Transactions) if the transactional information were on file on Form 8-K and incorporated by reference into the written confirmation or other selling literature.

3. "Company-Lite". In view of the ability of participants in the Company Registration system to exclude the placement of straight debt from the registration process and to conduct limited placements of securities to accredited investors, we question whether issuers need to be afforded the option of preserving transactional exemptions such as private placements for equity offerings. We are not convinced that the potential benefits of "company-lite" outweigh the disadvantages of the added complexity to the system and the continuation of such concepts as restricted securities, integration (albeit limited to private placements), general solicitation, etc.

4. Disclosure Enhancements. Although we support the concept of disclosure enhancements for Exchange Act filings, and agree in general with the recommendations of the Advisory Committee, we question whether the Management Report to the Audit Committee should be adopted as a mandatory feature of the system at this tune. A number of members of our Committee have expressed concerns as to the relative benefits of such a report as compared with the potential liabilities created by the requirement to file the report with the SEC, in addition to the added cost and expense, particularly with respect to the need to set forth procedures adopted by the company to deter and/or detect insider trading abuses.

5. Liability. One of the most complex and controversial areas that we believe requires further examination in connection with any effort to reform the registration and disclosure process is that of liability. The shift in emphasis under the Company Registration model from Securities Act disclosure to disclosure pursuant to Securities Exchange Act of 1934 (the "Exchange Act") has resulted in questions as to whether the current liability structure is consistent with the objectives of investor protection and regulatory simplification. The streamlining of the registration process also leads to questions as to whether the independent "gatekeepers" will be able to satisfy the present statutory standards of due diligence and will share the appropriate level of risk. The Separate Statement recognizes that liability issues may not only deter issuers from opting into the Company Registration system but also may inhibit the adoption of certain of the reforms proposed by the Wallman Report, such as the Disclosure Committee of outside directors. Further, while Company Registration as well as other initiatives would expand the use of written materials designed to provide the type of information to investors and the market that goes beyond the information customarily contained in the traditional prospectus (such as forward-looking information), it has been suggested that the use of meaningful selling literature, particularly materials that might involve the input of analysts, will not be utilized

by issuers and underwriters unless the subject of liability is adequately addressed. Our Committee has not reached a consensus at this tune as to the reforms to be recommended in this area. Suggestions have ranged from (1) eliminating Section 11 liability in Securities Act filings in exchange for an increase in liability for Exchange Act filings by adopting a uniform negligence standard under both Acts, to (2) limiting Section 11 liability to certain "core" information, such as Form 10-K, while providing a more relaxed negligence or fraud standard for both transactional information and "free writing" by issuers and underwriters, to (3) relaxing the current liability system or providing safe harbors only for gatekeepers such as underwriters and, possibly, for directors of an issuer that adopts a Disclosure Committee, to (4) adopting the liability scheme recommended by the Advisory Committee. As noted above, in light of the recently enacted National Securities Markets Improvement Act of 1996, together with the passage of the Private Securities Litigation Reform Act of 1995, it would appear that the Commission now has adequate exemptive authority to fully examine the liability provisions of both the Securities Act and the Exchange Act in an effort to accommodate the reforms of the Company Registration model.

III. SECURITIES ACT CONCEPTS

The Commission seeks comment on the best methods for eliminating unnecessary obstacles to capital formation while improving the quality and timing of disclosure and, therefore, investor protection. We believe that one of the principal objectives of the Commission should be to foster consistency and predictability in the implementation of the concepts applicable under both the Securities Act and the Exchange Act. Since there are numerous possible approaches to the issues addressed in this section of the Concept Release, we believe one of the primary objectives should be to establish a clear cut set of standards. We also note that even if a Company Registration system is adopted in the manner contemplated by the Wallman Report, a dual system will nevertheless be required to accommodate not only Initial Public Offerings ("IPOs") but also the primary and secondary trading of securities of companies not yet eligible to participate in Company Registration.

1. Quality of Ongoing Disclosure -- Timeliness of Disclosure. We concur in the conclusion of the Wallman Report that, as a general rule, a difference exists in the quality of disclosure in Exchange Act documents as compared to Securities Act documents. We therefore support the concept of disclosure enhancements to Exchange Act filings in order to improve the level of information available to the secondary trading markets. We endorse the views set forth hi the Separate Statement that to further strengthen the Exchange Act disclosures and to avoid "adopting company registration via the backdoor", many of the Exchange Act disclosure enhancements included hi the Company Registration system,

including the mandatory Form 8-K filing for non-de-minimis offerings, should be adopted at this tune. We also note that one of the major "enhancements" that would result from the adoption of the Company Registration model would be increased SEC Staff review of Exchange Act filings.

We strongly disagree, however, with any suggestion that there be a legal requirement that information that could materially affect the market for an issuer's securities be disclosed promptly in a public filing with the Commission. Listed companies already are subject to comparable requirements under the rules of the major stock exchanges, but with qualifications (many of which are subjective) to the general policy of prompt public disclosure. For example, Section 202.06 of the New York Stock Exchange Listed Company Manual states that "[j]udgment must be exercised as to the tuning of a public release on those corporate developments where the immediate release policy is not involved or where disclosure would endanger the company's goals or provide information helpful to a competitor". Further, the requirements of the stock exchanges do not create a private right of action for investors. Thus, although the addition of the specific items to Form 8-K recommended by the Advisory Committee may be desirable, as well as an acceleration of the filing period, the potential liability created by a general mandatory disclosure requirement without clear-cut evidence of abuse by reporting companies would not only be unwarranted but might result hi costly litigation far outweighing the potential benefits to investors.

2. Informing Investors; Informing the Market. Since the Wallman Report addresses these issues under the Company Registration model, and since any conclusions on this subject may very well depend upon the status of the particular issuer, we would not recommend any changes in this area, other than as part of a Company Registration pilot program as contemplated by the Wallman Report. We believe that virtually all of the questions raised in these sections of the Concept Release would be best left for further examination after a trial period under the Company Registration pilot program. However, with respect to the timing of prospectus delivery, we note that a mechanism would have to be developed under the Company Registration model for providing pricing information of the type currently covered by Rule 430A at the tune of the sale of securities but without any significant delay between the tune the pricing decision is made, the tune the market is informed and the tune of confirmation of sale. Since such pricing information generally is not available until immediately prior to sale, it may not be feasible to provide meaningful lead tune to the market.

3. The Role of Gatekeepers. With respect to the role of gatekeepers, we also concur in the Separate Statement that the transition from a transaction-oriented disclosure system to a Company Registration system should be accompanied by a corresponding transition in liability rules, such as a safe harbors, burden

shifting rules or clearer SEC guidance, as discussed in Appendix B of the Wallman Report.

4. Staff Review. For those issuers (other than IPOs) which are not eligible for Company Registration, we strongly support any steps to enhance the consistency and predictability of Staff review. We therefore support the suggestion contained in the Concept Release that the Commission consider making public the criteria used to determine whether to review repeat issuers' registration statements. We would not at this point recommend a shift to increased review of Exchange Act reports from Securities Act registration statements for those companies not electing to participate in Company Registration.

IV. COMMENTS ON ASPECTS OF SPECIFIC APPROACHES

As noted above, we recommend the adoption at this tune of a Company Registration system as a voluntary, pilot program in the form contemplated in the Wallman Report. We therefore support in general the recommendations of the Wallman Report with respect to the Scope of the System and Disclosure Enhancements.

Since we also support the Separate Statement, we would not recommend the adoption of the Task Force Report's recommendations for reforming the regulatory system, other than those reforms recommended by the Wallman Report and adopted as part of the Company Registration pilot program. As the Separate Statement suggests, both the need to adopt mandatory disclosure enhancements in conjunction with any relaxation of the existing shelf registration system and the need to incentivize eligible issuers to opt into the Company Registration model dictate against the piecemeal deregulation of the existing shelf registration system outside the Company Registration model at this tune.

Notwithstanding the foregoing conclusions with respect to specific approaches, a number of questions raised in this Section of the Concept Release address areas that have been colloquially identified as "33 Act metaphysics". As to these items, as noted below, we believe liberalization and/or rationalization at this tune would not negatively impact either the Company Registration model or the goal of investor protection envisioned by the Securities Act.

1. Revisiting Rule 152. We support the recommendation of the Task Force that Rule 152 be revisited to permit a company to switch from a private offering to a public offering without an intervening termination of the private offering. Similarly, we believe the Commission should modify its view that the act of filing a registration statement in connection with a non-shelf offering is deemed to

commence a public offering when the issuer has "quietly" filed a registration statement and no marketing effort has taken place. The Commission also should clearly define what constitutes a "quiet" filing, e.g., no general circulation of red herrings. We believe the Commission's current policy in this regard is unduly technical and imposes limitations on the capital raising process without benefiting investors.

2. General Solicitation; Testing The Waters. We believe the practical realities of the marketplace and the expansion of the public availability of information through electronic and other means has rendered the present concept of "general solicitation" an anachronism. We believe the elimination of the concept of general solicitation would be appropriate, at least on a limited basis, and we therefore support the extension of the approach of Rule 1001 to offerings on a nationwide basis; we support a broader relaxation of the general solicitation prohibitions for offerings made under Rules 505 and 506; and we support the "pink herring" concept, notwithstanding that we question the likelihood that a significant number of companies will adopt this approach to registration, especially since we believe that the filing should include limited company information as well as limited transaction-specific information. As noted in Subsection 1 above, we do not believe the mere filing of a registration statement should result in a per se conclusion that a company is engaging in general solicitation activities.

3. Liberalizing The Resale Of Unregistered Securities. While we question the desirability of piecemeal deregulation of the current registration system, we have no conceptual objection to expanding the group of eligible QIBs notwithstanding that we are not in a position to recommend a new standard. We also note that Rule 144A contains its own "metaphysics" by being limited to resales versus the original issuance of securities. We suggest that this technicality be eliminated by adding a comparable private placement exemption for issuers under Regulation D, consistent with current practice, and by clarifying the standards for contemporaneous Rule 144A and Regulation D sales. In order to complete the process, we also recommend that objective standards be established for exempt resales comparable to those provided under Regulation D for original issuances, thereby eliminating the need to rely upon the construct of Section "4 (1 1/2)".

Further, we doubt that reducing the Rule 144 holding periods to one and two years, respectively, would have any adverse effect on the current regulatory system or its integrity. In fact, we believe the realities of the marketplace suggest that in today's environment, holding a security for as long as one year clearly evidences the investment intent necessary to avoid underwriter status. Moreover, a reduction of holding periods may very well result in cost savings in the capital raising process.

4. The Four-Part Approach. Although we endorse many of the concepts recommended in this proposal, we note that Company Registration addresses not only those concepts, but many others that would not be covered by the implementation of these limited reforms. Thus, if the Company Registration model is adopted, the recommendations of the Four-Part Approach would be subsumed within the new system. However, as noted earlier in connection with our support of the Separate Statement, we would not at this tune recommend the adoption of these proposals other than as part of the Company Registration model or in response to the resolution of the limited issues identified in Subsections 1 and 2 above.

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We hope that the Commission will find these comments helpful. We also anticipate participating in the comment process with respect to the rulemaking proposals resulting from the Concept Release and the specific details of a Company Registration model. The undersigned would be available at the Commission's convenience to discuss further any aspect of these comments.

Respectfully submitted,

COMMITTEE ON SECURITIES REGULATION

By:
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Chairman of the Committee

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