April 28, 2000

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

**Re: Selective Disclosure and Insider Trading; Release No. IC-24209; File No. S7-31-99**

Dear Secretary Katz:

Please accept this comment letter on behalf of the North American Securities Administrators Association ("NASAA")[1] regarding the above-referenced release (the "Release"). NASAA would like to commend the staff of the Division of Market Regulation for proposing a pragmatic approach towards an important topic with such vast investor protection repercussions. In today's fast-moving and Internet-driven economy, it is important to level the playing field between the investing public and those who have traditionally been privy to and gatekeepers for material nonpublic information regarding publicly traded companies.

In the past, there was a rationale for selective disclosure. There were fewer markets, fewer market analysts and fewer market participants. Disclosing information to a select few analysts via a teleconference or a personal meeting may have provided the information to the market professionals who, for the most part, covered a security. Today, this rationale for selective disclosure no longer exists. There are more marketplaces where investors can participate and analysts are not the only sources for evaluating a security. In addition, as the Commission points out, new methods of communication are available today to minimize or eliminate the costs often associated with wide distribution of information to the public. Such wide distribution is necessary in part because of the tremendous increase in public involvement in the markets.

[1] NASAA is the association of the 66 state, provincial and territorial securities regulatory agencies of the United States, Canada and Mexico. NASAA serves as a forum for state regulators to work with each other in an effort to protect investors at the grassroots level and to promote fair and open capital markets.

While it has been argued that selective disclosure, or "tipping," promotes insider trading, the United States Supreme Court in *Dirks*[2] held that a person may lawfully trade using material nonpublic information unless it was made available "improperly." We support the Commission's approach to resolving this conflict left by *Dirks* by requiring full and fair disclosure.

Regulation FD

By setting out a proposed rule under Regulation FD ("Reg FD"), the Commission attempts to provide the public with better access to issuer information and to address the fairness problems surrounding selective disclosure of material nonpublic information. Under Reg FD, generally whenever an issuer, or any person acting on its behalf, discloses material nonpublic information to any person outside the issuer, the issuer must either simultaneously make public disclosure of that same information, if the disclosure was intentional, or the issuer must promptly make public disclosure of that same information, if the disclosure was non-intentional.

*Disclosures by "An Issuer or Person Acting on its Behalf"*

NASAA appreciates the difficulty in attempting to define to whom and when the proposed rule would apply. Individuals act, not entities. The actions of an entity are based upon the actions of an individual "authorizing" or performing the action. Thus, for the proposed rule to work, it must apply to individuals as well as entities and yet not be so broad and apply to so many individuals to be impractical to police by the public companies.

Under proposed Reg FD, the Commission proposes to define "person acting on behalf of an issuer" as "any officer, director, employee, or agent of the issuer who discloses material nonpublic information while acting within the scope of his or her authority." Although we believe this approach rightfully would not hold an issuer liable for an employee's ill deeds outside of his or her position within the issuer company, we see a potential loophole should this approach be used. The issuer could make a general policy statement to the effect that whenever an employee provides selective disclosure pursuant to this proposed rule, the employee is acting outside his/her scope of authority. Thus, only the employee, individually, could be held liable, not the issuer, even if the issuer encouraged the disclosure.

Alternatively, the Commission offers a broader definition of "person acting on behalf of an issuer" to cover "any person authorized to act on behalf of the issuer." Given the possible loophole described above, NASAA is more supportive of this definition because it puts the burden on the issuer to regulate and identify those persons who would most likely be in possession of and have responsibility to disclose material information to the public. However, usage of the term "authorized" is not definitive enough and may not prevent evasion. Within this context, "authorized" is not an intuitive term; a person needs to know if and how they are authorized to act on behalf of the issuer. We would

[2] Dirks v. SEC, 463 U.S. 646 (1983).

respectfully recommend the Commission provide guidance as to how it would interpret who would be "authorized." For example, would the Commission look to a corporate job description?

*Disclosure of Material Nonpublic Information*

Reg FD only applies to disclosure of "material" nonpublic information. Therefore, disclosures that are not "material" themselves and disclosures of strictly public information are not the concern here. In addition, Reg FD does not require issuers to disclose all material information. Rather, the proposal requires that when the issuer chooses to disclose such material information, it do so publicly.

The Commission does not define the term "material" for Reg FD, but relies on the general definition espoused by the United States Supreme Court in TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976), which states information is "material" if "there is a substantial likelihood that a reasonable shareholder would consider it important, in making an investment decision, or if it would have significantly altered the 'total mix' of information made available." NASAA supports the Commission's decision to rely upon this definition. Materiality is a concept that pervades most, if not all, areas of securities law. An attempt by the Commission to define "materiality" for the purposes of Reg FD could have broader implications.

We agree with the Commission that materiality judgments cannot always be readily determined. Materiality is a facts and circumstances determination. Although some delay in the flow of information to the marketplace may occur while such determinations are made, NASAA believes that the proposed rule strikes the right balance between fostering the continuous flow of information to the marketplace and fair and full disclosure to all investors. In addition, the proposal provides an issuer the ability to take corrective action for unintentional selective disclosures.

The Commission also asks for comment on whether the term "public disclosure" should be further defined. We believe that a further definition is not necessary, as rule 101(e) sufficiently sets out a standard.

*Selective Disclosure "To Any Other Person Outside the Issuer"*

Reg FD covers selective disclosure made "to any other person outside the issuer." Thus, Reg FD does not apply to communications among an issuer's employees, but only to communications of material nonpublic information to outsiders such as certain investors and outside analysts.

NASAA generally agrees with the Commission's suggestion that proposed Reg FD not apply to disclosures of material nonpublic information to those with duties of "trust or confidence" not to disclose or use such information for trading. We recognize the need for having issuers communicate with certain individuals such as attorneys, outside consultants and accountants, especially in light of the due diligence that is necessary to

prepare required filings under the Commission's rules and for public offerings and merger situations. However, to avoid nullifying the intent of this proposal, we support, at a minimum, that sharing of material nonpublic information under such circumstances be permitted only if disclosed pursuant to a written agreement.

*Timing of Public Disclosure Required by Regulation FD*

If an inappropriate selective disclosure has been made by an issuer, the proposal draws a distinction between how the disclosure occurred and what appropriate follow up public disclosure must occur. The issuer must either simultaneously make public disclosure of that same information if the disclosure of material nonpublic information was intentional or the issuer must "promptly" make public disclosure of that same information if the disclosure was non-intentional.

We believe the distinction between "intentional" and "non-intentional" disclosures is appropriate. NASAA supports the requirement for "simultaneous" disclosure to the public for intentional selective disclosures. Simultaneous disclosure of the information is not too burdensome for the issuer in light of the many economical methods available today for broad dissemination of information. Reg FD was proposed for investor protection reasons and to level the playing field by providing public access to material information. The need for timely and full disclosure outweighs the cost that must be borne by issuers that have affirmatively chosen to make selective disclosures.

Under the proposal, if an issuer makes an "non-intentional" disclosure, the issuer must publicly disclose the same information "promptly." "Promptly" is defined as "soon as reasonably practicable (but not later than 24 hours) after a senior official (any executive officer of the issuer, any director of the issuer, any investor relations officer or public relations officer, or any employee possessing equivalent functions) of the issuer knows (or is reckless in not knowing) of the non-intentional disclosure." Although the proposal ties the timing of the required public disclosure after a unintentional selective disclosure to when a broad spectrum of persons within an issuer either become aware or should be aware of the selective disclosure, we are concerned the phrase "or any employee possessing equivalent functions" is too narrow. We respectfully suggest the Commission consider broadening the definition to specifically include additional categories of middle management that may be authorized to make disclosures on behalf of the issuer and therefore would know or should know if an improper selective disclosure has been made.

*Definition of "Public Disclosure"*

Reg FD allows the issuer to publicly disclose material nonpublic information either by filing a Form 8-K, disseminating a press release or disseminating the information through a method of broad public access such as a press conference. While NASAA generally agrees with the methods Reg FD proposes for public disclosure, we have the following comments and suggestions.

We recommend the Commission consider providing more requirements or guidance regarding the use of press conferences as a means of public disclosure. We are concerned that permitting the use of press conferences if they allow broad public access may be insufficient as a means of insuring the public can obtain effective access to the information that is the basis of the selective disclosure. We urge the Commission to set up minimum parameters regarding access to and usage of press conferences. For example, an issuer relying upon a press conference should have to demonstrate that telephonic or electronic access is reasonably attainable by the public who indicate to the issuer they want access to the press conference (e.g., equipment necessary for connection to the transmission must be reasonably available and telephonic connections must provide an effective means for those listening to hear the announcements).

NASAA agrees with the Commission that a posting by an issuer on its web site of the information that was the basis of the selective disclosure alone is insufficient as a means of public disclosure. The burden should not be placed on investors to discern if an issuer has made a selective disclosure. If web site posting alone were a permitted means of public disclosure, an investor would have to continuously check issuers' web sites. However, we suggest that if an issuer has a web site, it must also post the information on the site in addition to using another one of the outlined methods of disclosure to the public.

We support the Commission's suggestion for a delayed Form 8-K filing. The purpose of reporting on EDGAR is to have material information about a reporting company accessible from a central place. The Form 8-K was implemented because quarterly 10-Q filings did not provide sufficient, timely information to the market regarding material company changes. Thus, to further the purpose of proposed Reg FD, an 8-K filing should be required. In addition, NASAA supports a separate item 10 be added to Form 8-K for Reg FD disclosures to distinguish the disclosures made pursuant to Reg FD from the optional reporting permitted under item 5 on Form 8-K.

We would also recommend the Commission consider precluding an issuer from "curing" a selective disclosure by selectively publicly disclosing or using differing forms of public disclosure for different audiences. For example, an issuer should not hold a conference call for analysts as a means of public disclosure and rely upon an 8-K filing for public disclosure for the remaining interested parties.

*Liability Issues and Securities Act Implications*

With respect to issuers that have already filed a registration statement, the Commission proposes Rule 181 to allow such issuers to make the required Reg FD public disclosures without violating Section 5(b)(1) of the Securities Act and thus having to comply with the prospectus requirements of Section 10 of the Securities Act. We support proposed Rule 181. We also support extending the application of the rule only to non-intentional disclosures. By applying the rule only to non-intentional disclosures, there is less

likelihood that issuers will take advantage of this rule to hype an offering of securities while in the registration process but avoid any Section 10 prospectus requirements.

In addition, we urge the Commission to require any material nonpublic information disclosed during the "waiting period" to be included in the registration statement at the time it is declared effective. Investors should expect to receive all material information in the final prospectus rather than having to cobble together various disclosures by the issuer to get a "full" picture of the company.

Finally, we support the Commission's decision not to adopt an exemption from liability from Section 5(c) for communications made before the filing of a registration statement. As the Commission points out in the release, "companies could abuse that exemption to make public communications that hype an offering before filing a registration statement with the Commission [and] …balanced full disclosure, against which to test the hyping information, would not be available" (because the registration statement has not been filed.) The possible harm to investors based on partial information could be significant. In addition, we support not applying Reg FD to issuers engaged in Initial Public Offerings for the same reasons as stated above relating to an issuer that has not yet filed a registration statement. Investors will not have the benefit of being able to judge the mandated public disclosure against a regulatory filing that has been vetted.

INSIDER TRADING ISSUES

In general, NASAA supports the SEC proposal regarding Rule 10b5-1, trading on the basis of "material nonpublic information," as well as Rule 10b5-2, duties of trust or confidence in misappropriation insider trading cases. We realize this is an area of the law where further guidance is necessary and we support the SEC's need for clarification.

In conclusion, NASAA supports the Commission's proposed rules regarding Selective Disclosure and Insider Trading. The rules bring a degree of fairness and transparency to the disclosure of material information. Today, such material information is often received too late by investors for them to be able to act on it in their best interest. We are also pleased that the proposed rules not only allow for efficient and timely dissemination and transmission of material information, but they do not appear to unduly burden the issuer. If you have any questions or if NASAA can be of further assistance, please do not hesitate to contact me directly, at 317-232-6095, or Karen O'Brien at the NASAA corporate office at 202-737-0900.

Respectfully Yours,

Bradley W. Skolnik
NASAA President