



QUICK REFERENCE GUIDE
SEC REVIEW
PROCESS



Every public company has its filings with the SEC scrutinized at least once every three years.

A FEW COMMENTS ON COMMENT LETTERS

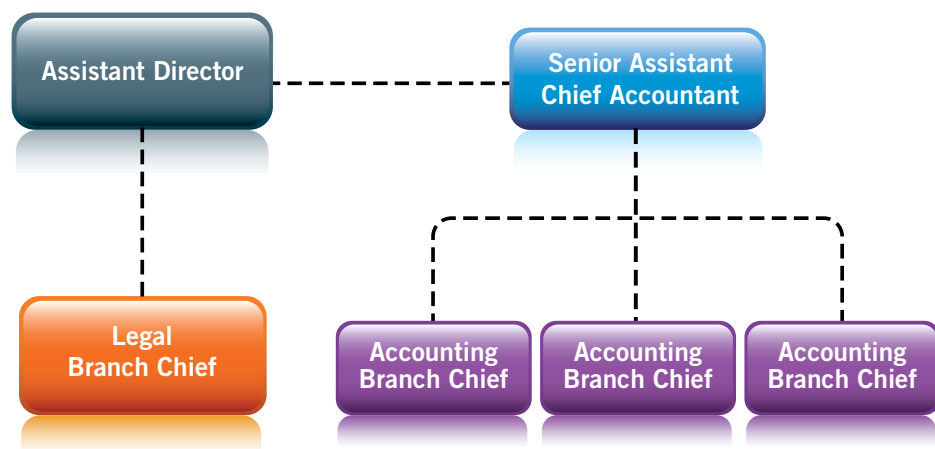
A review of SEC filings is about as welcome as an IRS audit but occurs with greater frequency and predictability. Every public company has its filings with the Securities and Exchange Commission (SEC) scrutinized at least once every three years. As the SEC reviews company filings, whether on a routine or selective basis, it often issues a comment letter to which the recipient company must respond post haste. Want to understand how the SEC review process works and what to expect if your company receives a comment letter? Read on.

ORGANIZATION

The SEC's Division of Corporation Finance reviews public filings. Most of the Division's staff is concentrated in 11 field offices; the Division assigns review work to 11 Assistant Director Offices (ADO). Each ADO is assigned to one of the following industries:

- ▶ Health care and insurance
- ▶ Consumer products
- ▶ Computers and online services
- ▶ Natural resources and food
- ▶ Structured finance
- ▶ Transportation and leisure
- ▶ Manufacturing and construction
- ▶ Financial services, real estate and business services
- ▶ Beverages, apparel and health care services
- ▶ Electronics and machinery
- ▶ Telecommunications

Each ADO is organized as follows:



Each ADO is staffed with 25 to 35 professionals, mostly accountants and lawyers. Each public company's ADO assignment is shown in EDGAR after the basic company information that precedes the company's filing history. Each of the 11 ADOs has up to three Accounting Branch Chiefs reporting to one Senior Assistant Chief Accountant. An Associate Director (Karen Garnett, Paul Belvin, Mark Kronforst, James Daly or Barry Summer) oversees each ADO. The Acting Director (Shelley Parratt) oversees the entire filing review process.

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The Associate Directors and Ms. Parratt supervise the Assistant Directors and are not depicted in the above organization chart. Also not depicted in the organization chart above are the Associate Chief Accountants in the SEC’s Office of the Chief Accountant, who serve as liaisons for each ADO; and Wayne Carnall, the Division of Corporate Finance’s Chief Accountant, who is the principal advisor to Ms. Parratt.

REGULATORY REVIEW

Public filings are reviewed in accordance with the Sarbanes-Oxley Act of 2002 (SOX). Under SOX Section 408, the SEC must review every public company once every three years. The staff also performs selective reviews of transactional filings, such as those for public offerings, business combinations and proxy solicitations. The SEC has never revealed the mechanics of the selective review process. If the SEC decides to perform a selective review, it may focus on a particular disclosure issue or the review could encompass the entire filing.

Reviews are conducted by asking questions that a potential investor might ask. The SEC completes many filing reviews without issuing comment letters, but when the SEC thinks a company should enhance or amend its filing, it provides a comment letter. An Examiner and a Reviewer are the initial points of contact. The Reviewer approves all proposed comments.

THE DIALOGUE

The comment process is a dialogue with a company about its filing. The SEC’s comments are based on the staff’s understanding of the company’s facts and circumstances. The SEC may request supplemental information that can be used for many purposes, including obtaining a better understanding of the company’s current disclosure or a future filing, or obtaining information to revise disclosures in a document on file with the SEC.

When a company receives a comment letter, it generally is expected to respond to each comment. If necessary, the company will amend its filing. The company’s explanation or analysis often resolves the issue on which the comment is based, often without further dialogue. However, the SEC may issue additional comments after it reviews the company’s responses to prior comments. The dialogue continues until the SEC and the company completely resolve all comments. In cases where the SEC and the company disagree with the outcome, companies are invited to make an appeal (*see below*).

When a company has resolved all SEC comments on a Securities Act registration statement, the company may request that the SEC declare the registration statement effective, in order to proceed with the transaction. The SEC does this by giving public notice on EDGAR. When a company has resolved all SEC comments on an Exchange Act registration statement, a periodic or current report (i.e., 10-Q or 10-K), or preliminary proxy statement, the SEC will provide the company with a “no further comment” letter to confirm that its review of the filing is complete.

PUBLIC INFORMATION

Not only will your comment letters go public, your responses will end up public, too. When the SEC completes a filing review, it makes comment letters and company responses public on EDGAR, including the “no further comment” letter. This is done no earlier than 45 days after the SEC has completed its review of a periodic or current report or declared a registration statement effective. However, the SEC redacts (i.e. revises) any information that

is subject to a company's Rule 83 confidentiality request. Companies may therefore ask that sensitive portions of their responses be revised. Such requests are regularly granted without substantive evaluation but are subject to the Freedom of Information Act. When making a Rule 83 request companies usually must file a "Tandy letter" indicating that the SEC's comments may not be used as a defense in a legal proceeding.

THE APPEALS PROCESS

If a company does not understand a comment or its intent, clarification should be sought from the Examiner before responding. If the company still has questions after discussions with the Examiner, a company representative may speak to the Reviewer who approved the comment. The SEC includes the names and phone numbers of the staff members involved in each comment letter. If the SEC suggests that a company revise its filing, the company should provide the staff with a written explanation of why it provided the disclosure it did. This is often enough to resolve the comment.

If the staff indicates that it plans to reissue the comment, the company may wish to have the situation reconsidered prior to such reissuance. If the matter will be appealed, the company should ask to speak to the Reviewer after working with the Examiner.

The SEC's comment letter appeal process is referred to as "reconsideration." There are two types of appeals and two types of appeals processes. The first deals with legal and textual disclosure matters, while the second provides for accounting and financial disclosure matters.

For legal and textual disclosures, a company should "normally" first reach out to the Legal Branch Chief. After discussions with the Assistant Director, the company may address it with the Associate Director who oversees that office (Karen Garnett, Paul Belvin, Mark Kronforst, James Daly, or Barry Summer). The appeals process does not end here. After that, companies are invited to discuss the matter with the Deputy Director (Shelley Parratt) or the Director. Each comment letter identifies one or more of the staff members assigned to each company's review. These staff members may include the Examiner and Associate Director.

The SEC's Web site emphasizes that there is no rigid approach to the appeals process. In fact, the appeals process is explicitly flexible. Staff members "at all levels" are available to discuss matters. A company "should not hesitate" to request that the staff reconsider a comment it has issued or reconsider a staff member's view of the company's response to a comment "at any point" in the filing review process. **The SEC does not require companies to follow a formal protocol in consulting with its staff or in seeking reconsideration of a staff comment.** A request for reconsideration may be either oral or written.

For accounting and financial disclosure issues, the normal course of reconsideration could begin with the Accounting Branch Chief (*see the organization chart above*). There can be up to three Accounting Branch Chiefs in each ADO. Each comment letter should identify the respective Accounting Branch Chief; if you are uncertain who it is, ask your Examiner. The next step could be to discuss the matter with the Senior Assistant Chief Accountant. Each of the 11 ADOs has up to three Accounting Branch Chiefs reporting to one Senior Assistant Chief Accountant. After that, a company may address the matter with the Associate Chief Accountant in the Division's Office of the Chief Accountant, who serves as the liaison for each ADO.

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The appeals process does not end here. A company may direct further reconsideration requests to the Division of Corporate Finance’s Chief Accountant Wayne Carnall. Companies should feel free to involve the Assistant Director, Associate Director or Acting Director at any stage. Companies are even invited to further reach out beyond the Division of Corporate Finance to SEC’s Office of the Chief Accountant, headquartered in Washington, D.C., at any stage in the process. Generally, the Office of Chief Accountant deals with the application of US GAAP, whereas the Division of Corporate Finance resolves format and content issues.

EXAMPLES OF SEC COMMENTS

Fair value accounting is one of about 25 main topics targeted by the SEC in its filing reviews, along with revenue recognition and impairments. Auction rate securities continue to be at the heart of many comments relating to fair value accounting:

- “ Clarify how you determined that a market was not active.”
- “ Disclose how the lack of liquidity impacted the valuation technique used, and how illiquidity was factored into the determination of fair value.”
- “ Explain why you believe yield curves and time value represent Level 2 inputs.”
- “ Provide your analysis regarding your determination not to bifurcate and account for the conversion feature as a derivative.”
- “ Expand your MD&A discussion of recent economic events and their current and expected future impact on your operations, financial position and liquidity.”
- “ Provide additional quantitative disclosures that convey to investors current and ongoing risks caused by business developments.”
- “ Provide more detailed disclosures regarding risks and exposures.”
- “ Describe the impact that the turmoil in the credit markets has had on your valuation of these (auction rate security) investments and how you considered addressing these matters for your investors.”

In the current economic environment, liquidity has decreased and inactivity in markets has increased. The result is that data points used in valuation models have become less observable. As such, valuations require subjective analysis; the SEC expects more transparency when supporting amounts on the balance sheet.

CONCLUSION

The probability that your company, or a competitor in your industry, will need to respond to an SEC comment letter is high. Many of the 25 main topics targeted by the SEC can be handled with internal legal accounting and legal advisors, however, some of them, including fair value accounting, are best handled with the assistance of an outside valuation firm. The best way to prepare for an SEC comment letter is to align your company with an independent third party valuation firm that can assist you in responding to any potential SEC queries. Pluris monitors SEC comment letter developments and understands the issues and pitfalls companies face.

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