



# TOP 10 PRACTICE TIPS: RESPONDING TO SEC COMMENT LETTERS

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This practice note outlines 10 practice points for public companies to consider when responding to comment letters from the Securities and Exchange Commission (SEC). The SEC is required to review the SEC filings of public companies at least every 3 years and sometimes does so more frequently. Companies with large market capitalizations, material restatements, or market volatility may be reviewed annually or even continuously. It is also almost automatic to receive comments in an initial public offering (IPO) or in connection with the merger or sale of a publicly traded company. The scope of SEC review can range from 20 or more comments on a variety of topics in an IPO to a single comment on a Form 10-K regarding a specific issue. Legal compliance comments tend to be more infrequent and easier to deal with than accounting comments, which often require significant analysis of technical accounting rules, second guessing of judgments, or even revision of financial statements.

When you receive a comment letter, don't panic. The process can be smooth if you are prepared. Responding to an SEC comment letter can be more art than science, but below are some best practices to follow:

## 1. READ THE COMMENT LETTER CAREFULLY, AND ANSWER EVERY QUESTION AND SUB QUESTION IN IT.

Be sure to read the comment letter carefully to understand exactly what the SEC is asking, paying particular attention to whether the comment is requesting updates in future disclosure, supplemental information, or revision to a current filing. SEC comment letters often contain multiple comments each with several sub-questions. It is important to review each comment thoroughly and be sure to respond to each portion of the question or request. This makes it easier on the SEC staff and helps prevent a second round of comments.

With respect to comments on registration statements, the SEC typically asks for revised disclosure in the form of an amendment to such filing. As a courtesy, send redline copies of the amendment to the SEC reviewers via overnight mail or courier.

## 2. PICK YOUR BATTLES.

You should be strategic in acquiescing to or fighting a comment. You need not assent to every request in an SEC comment letter as there is often room for debate or discussion with the SEC staff. It is fine to disagree with the staff and put forth arguments on why your approach is correct. That said, in order to avoid additional rounds of comments and to save your credibility for more significant

disputes, it is often easier to agree to comply with minor comments or requests that can painlessly be implemented even if you may not agree with the SEC's position.

## 3. IT DOESN'T HURT TO CALL THE SEC STAFF.

Companies are sometimes reluctant to call the SEC staff. However, if a comment is unclear, it is appropriate to call the SEC staff member listed on the comment letter for clarification. It is often better to ask the SEC for clarification rather than responding to the comment without fully understanding it and, therefore, increasing the likelihood of a second round of comments. Sometimes the SEC staff may be unwilling to discuss its reaction to your response until they see it in writing, but they are typically willing to speak about the substance of the comment after you submit an initial response, or if you receive a follow-up comment. These conversations can clarify the staff's point of view, eliminate confusion, allow each side to ask helpful questions, and allow you to explain your position in a way that may be difficult to convey in writing. You should also include outside counsel on the call to leverage their regular experience with the staff and provide a potential buffer for any debates.

## 4. ASSEMBLE THE RIGHT TEAM TO COMPLETE THE RESPONSE.

In order to efficiently and effectively respond to SEC comments, organize the appropriate internal and external team to address the particular comments. Typically, someone

from the internal legal or accounting department would lead the process. The team should include applicable internal subject matter specialists, outside counsel, and external auditors. They can be a useful resource in responding to comments as they have likely seen many more comments from working with a variety of companies (or in the case of internal subject matter specialists, a deep knowledge of the comment's topic ) giving them experience to guide you through sensitive issues with the SEC. In addition, it is important to get the external auditors involved early if the comments relate to accounting issues and methods. The external auditors will need to concur on any changes in accounting methods, and if the comments relate to registration statements, will need to give another consent when amending the registration statement. It is also important to inform the company's audit committee early in the process of the comment letter and to keep them abreast of the responses, particularly if the comments relate to financial reporting or accounting disclosure.

## 5. FOCUS ON GETTING THE COMMENT RESPONSE(S) RIGHT RATHER THAN THE DEADLINE TO RESPOND.

The comment letter will typically state that you have you 10 business days to respond to the comments. However, don't hesitate to ask the SEC for additional time to respond. As noted below, remember that all responses to comment letters will eventually be made public. Poorly drafted responses, insufficient answers, and protracted exchanges with the SEC on issues can lead to additional comments and reflect poorly on the company. It is almost always better to take the time to craft well thought-out responses rather than rush the process.

The SEC will usually grant an extension to respond in up to 20 business days. If you believe you will need additional time, contact the SEC staff sooner rather than later to request an extension. Make sure to pick a reasonable time to respond based on your circumstances so as not to pester the staff with multiple extensions. Keep in mind that the SEC staff will often direct you to file correspondence on EDGAR stating when you will respond to the comments.

## 6. REMEMBER THAT ALL COMMENT LETTERS AND RESPONSES WILL EVENTUALLY BECOME PUBLIC. SEEK CONFIDENTIAL TREATMENT FOR RESPONSES WHERE APPROPRIATE.

All correspondence to or from the SEC (i.e., comment letters and responses) are posted to EDGAR no earlier than 20 business days after the SEC completes its review, which is the time that all comments from the SEC have been resolved. You should be aware that shareholders, employees, and members of the media will be able to see the full back and forth with the SEC. Public scrutiny of the comment dialogue could be particularly sensitive if the comments relate to controversial issues or if you are considering an offering or other major transaction in the future.

Keep in mind that if there is confidential or sensitive information in your responses to the comments, you may be able to request confidential treatment of certain portions of the responses under Rule 83 (17 C.F.R. § 200.83) of the SEC's Rules of Practice. Under Rule 83, you may redact certain portion(s) of the responses filed on EDGAR if you follow the exact procedures set out in the rule. Note also that confidential treatment requests under Rule 83 do not require you to substantiate the legal arguments for confidentiality at the time of your submission. Under Rule 83, the SEC staff does not make a determination whether the information will be kept confidential until, if and when, a Freedom of Information Act (FOIA) request for the information is actually submitted. If a FOIA request is made for the redacted information in a comment response letter, the SEC will notify the company and ask for arguments on why such information should be kept confidential before making its determination on whether to release the redacted information. Even though the SEC will not ask for substantive confidentiality arguments at the time of submission of a comment letter, it is good practice to prepare a memo or other notes outlining the rationale for confidentiality so that you are prepared if a FOIA request is made, especially because a FOIA request can be made years later.

## 7. KEEP YOUR PROMISES ON FUTURE DISCLOSURES.

The SEC may ask for, or you may voluntarily provide, sample future disclosure in your responses. Responses will also often include commitments to disclose particular information in the future. As a result, prior to submitting your responses, make sure your full SEC disclosure team is comfortable with any sample future disclosure and commitments. It can be embarrassing (and frustrating to the SEC) to receive a future comment asking that you comply with your previous promise made in a prior comment response letter. In order to make sure prior comment responses are fully incorporated into your SEC filings, the internal team and outside counsel should review prior comment response letters as part of their Form 10-K and 10-Q compliance checks.

## 8. ESCALATE WHEN NECESSARY.

Carefully consider when to appeal above the initial SEC reviewer's head. If no resolution can be achieved with respect to a particular comment or if the company wants to press a policy argument, it may be necessary to move up the ladder of the SEC reviewer hierarchy (e.g., Assistant, Associate, or Deputy Director for legal comments; Accounting Branch Chief, Senior Assistant Chief Accountant, or the Office of the Chief Accountant for accounting comments).

Before you appeal, make a good faith attempt to resolve the comment with the initial SEC staffer listed on your comment letter. If resolution can't be achieved, explain professionally to the initial reviewer that you would like to speak with the next level in the SEC chain and ask if they would help to facilitate such conversation. It is always advisable to seek advice from your outside counsel and

external auditors on how to approach any escalation with the SEC in order maximize your chances for successful resolution.

## 9. PROVIDE SAMPLE DISCLOSURE WHEN APPROPRIATE, BUT LOOK AT PRECEDENT RESPONSES.

As discussed above, SEC comment letters will often request modified or additional disclosures, most often with respect to accounting disclosures. When appropriate (especially with controversial or complex disclosure), it is often advisable to include a proposed version of future disclosure in your initial comment response (as opposed to simply agreeing to include it in the next applicable SEC filing). That way, the SEC staff can comment immediately on any issues with your proposed disclosure, helping to streamline the process and avoid future follow-up comments.

Also remember that the comment you receive is typically not the first time that the SEC has issued that particular type of comment. Therefore, as part of your comment response process, it is helpful to review precedent responses from other companies for guidance. Precedent can help you see what arguments were and weren't successful, and help anticipate what the SEC may be looking for in response to a particular comment.

## 10. PREPARE FOR TRICKY COMMENTS.

The SEC typically focuses many of its comments on several current hot button issues (e.g., financial measures not in accordance with generally accepted accounting practices, fair value measurements and estimates, loss contingencies, or segment reporting, among others). Prepare for and preempt potential SEC comments before you file by knowing the current hot button issues and regularly reviewing comments and responses of your peers. To assist with a proactive approach to disclosure, several large accounting firms regularly publish information on the frequent topics and trends addressed in SEC comment letters.

In addition, whenever you are faced with difficult accounting or disclosure judgments, you should document your consideration and analysis of those issues in case you need to explain them to the SEC in a subsequent comment response. These actions can help you to craft current disclosure to avoid future SEC comments, and also prepare you to respond to potential future SEC comments.

### BONUS TIP: NO MORE TANDY LANGUAGE.

The SEC no longer requires companies to include the so-called Tandy representations in their comment response letters. Note that the SEC has made it clear that the absence of Tandy language does not change the SEC's position that the company essentially represents that it won't raise the SEC's comment process as a defense in securities litigation.