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March 16, 2012

The Honorable Dianne Feinstein
United States Senator for California
331 Hart Senate Office Building
Washington, D.C. 20510

Dear Senator Feinstein:

We are writing to you on behalf of the members of the California State Teachers' Retirement System (CalSTRS). CalSTRS was established for the benefit of California's public school teachers nearly 100 years ago and is currently the largest teacher pension system in the United States. The CalSTRS portfolio is currently valued at approximately \$152 billion and through this portfolio we strive to prudently serve the investment and retirement interests of our 856,000 plan participants. CalSTRS pays out over \$10 billion each year to retirees and their families across our State. CalSTRS is a fiduciary to the beneficiaries of this plan and it is with this duty in mind that we have been an active proponent of investor safeguards throughout our history. We are writing to express our opposition to the Jumpstart Our Business Startups Act (JOBS Act) and our support for the INVEST in America Act (INVEST Act) as its substitute.

While we agree that job creation and capital formation are both critical to our economic recovery, we do not believe the JOBS Act, in its current form, will achieve this important objective because certain provisions of the JOBS Act which roll back important investor protections will actually weaken market transparency and erode the public's faith in a market that appears to be on the cusp of a recovery. In fact, the Securities and Exchange Commission Chair shares our concerns as expressed in the attached letter from Ms. Schapiro to Senator Johnson, Chairman of the Senate Banking Committee. For investors, like CalSTRS, important statutory requirements over internal controls and advisory votes on compensation, which were put in place to mutually benefit issuers and investors, are essential for us to properly assess the risks in our portfolio.

We believe the INVEST Act goes a long way to addressing some of the concerns we have with the JOBS Act in its original form. Specifically, lowering the limit to qualify as an "emerging company" from \$1 billion in revenues to less than \$350 million in revenue provides for fewer exemptions from accounting rules and compensation requirements. In addition, the INVEST Act allows companies to "opt out" of the "emerging company" status and fully comply with all public company requirements. This inclusion is important to investors, such as CalSTRS, that often provide venture capital and private equity to

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companies that may go to the public markets for capital. It allows investors the opportunity to encourage companies to "opt out" of this classification and embrace these important investor protections as they are able. Finally, the INVEST Act will also continue to protect investors by insuring research used to advise investors is not tainted by conflicts of interest.

We appreciate the opportunity to express our views and respectfully request your support of the INVEST Act. If you would like to discuss this matter, please feel free to contact me at 916-414-2100.

Sincerely,



Jack Ehnes
Chief Executive Officer

Enclosures



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

THE CHAIRMAN

March 13, 2012

The Honorable Tim Johnson
Chairman
Committee on Banking, Housing, and Urban Affairs
U.S. Senate
534 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Richard C. Shelby
Ranking Member
Committee on Banking, Housing, and Urban Affairs
U.S. Senate
304 Russell Senate Office Building
Washington, D.C. 20510

Dear Chairman Johnson and Ranking Member Shelby:

Last week, the House of Representatives passed H.R. 3606, the “Jumpstart Our Business Startups Act.” As the Senate prepares to debate many of the capital formation initiatives addressed by H.R. 3606, I wanted to share with you my concerns on some important aspects of this significant legislation.¹

The mission of the Securities and Exchange Commission is three-fold: protecting investors; maintaining fair, orderly and efficient markets; and facilitating capital formation. Cost-effective access to capital for companies of all sizes plays a critical role in our national economy, and companies seeking access to capital should not be hindered by unnecessary or overly burdensome regulations. At the same time, we must balance our responsibility to facilitate capital formation with our obligation to protect investors and our markets. Too often, investors are the target of fraudulent schemes disguised as investment opportunities. As you know, if the balance is tipped to the point where investors are not confident that there are appropriate protections, investors will lose confidence in our markets, and capital formation will ultimately be made more difficult and expensive.

While I recognize that H.R. 3606 is the product of a bipartisan effort designed to facilitate capital formation and includes certain promising approaches, I believe that there are provisions that should be added or modified to improve investor protections that are worthy of the Senate’s consideration.

¹ The views expressed in this letter are my own and do not necessarily represent the views of the full Commission.

Definition of Emerging Growth Company

The “IPO On-Ramp” provisions of H.R. 3606 provide a number of significant regulatory changes for what are defined as “emerging growth companies”. While I share the view that it is important to reduce the impediments to smaller businesses conducting initial public offerings in the United States, the definition of “emerging growth company” is so broad that it would eliminate important protections for investors in even very large companies, including those with up to \$1 billion in annual revenue. I am concerned that we lack a clear understanding of the impact that the legislation’s exemptions would have on investor protection. A lower annual revenue threshold would pose less risk to investors and would more appropriately focus benefits provided by the new provisions on those smaller businesses that are the engine of growth for our economy and whose IPOs the bill is seeking to encourage.

Changes to Research and Research Analyst Rules

H.R. 3606 also would weaken important protections related to (1) the relationship between research analysts and investment bankers within the same financial institution by eliminating a number of safeguards established after the research scandals of the dot-com era and (2) the treatment of research reports prepared by underwriters of IPOs.

H.R. 3606 would remove certain important measures put in place to enforce a separation between research analysts and investment bankers who work in the same firm. The rules requiring this separation were designed to address inappropriate conflicts of interest and other objectionable practices – for example, investment bankers promising potential clients favorable research in return for lucrative underwriting assignments – which ultimately severely harmed investor confidence. In addition, H.R. 3606 would overturn SRO rules that establish mandatory quiet periods designed to prevent banks from using conflicted research to reward insiders for selecting the bank as the underwriter. I am concerned that the changes contained in H.R. 3606 could foster a return to those practices and cause real and significant damage to investors.

In addition, the legislation would allow, for the first time, research reports in connection with an emerging growth company IPO to be published before, during, and after the IPO by the underwriter of that IPO without any such reports being subject to the protections or accountability that currently apply to offering prospectuses. In essence, research reports prepared by underwriters in emerging growth company IPOs would compete with prospectuses for investors’ attention, and investors would not have the full protections of the securities laws if misled by the research reports.

Disclosure, Accounting and Auditing Matters

H.R. 3606 would allow emerging growth companies to make scaled disclosures, in an approach similar to that currently permitted under our rules for smaller reporting companies, and would provide other relief from specific disclosure requirements, during the 5-year on-ramp period. While there is room for reasonable debate about particular exemptions included in the

disclosure on-ramp, on balance I believe allowing some scaled disclosure for emerging growth companies could be a reasonable approach.

H.R. 3606, however, also would restrict the independence of accounting and auditing standard-setting by the Financial Accounting Standards Board (“FASB”) and the Public Company Accounting Oversight Board (“PCAOB”). These provisions undermine independent standard-setting by these expert boards, and both the FASB and the PCAOB already have the authority to consider different approaches for different classes of issuers, if appropriate.

Moreover, H.R. 3606 would exempt emerging growth companies from an audit of internal controls set forth in Section 404(b) of the Sarbanes Oxley Act during the five-year on-ramp period. IPO companies already have a two-year on-ramp period under current SEC rules before such an audit is required. In addition, the Dodd-Frank Act permanently exempted smaller public companies (generally those with less than \$75 million in public float) from the audit requirement, which already covers approximately 60 percent of reporting companies. I continue to believe that the internal controls audit requirement put in place after the Enron and other accounting scandals of the early 2000’s has significantly improved the quality and reliability of financial reporting and provides important investor protections, and therefore believe this change is unwarranted.

“Test the Waters” Materials

H.R. 3606 would allow emerging growth companies to “test the waters” to determine whether investors would be interested in an offering before filing IPO documents with the Commission. This would allow offering and other materials to be provided to accredited investors and qualified institutional buyers before a prospectus – the key disclosure document in an offering – is available.

There could be real value to permitting these types of pre-filing communications: it could save companies time and money, and make it more likely that companies that file for IPOs can complete them. Indeed, there are some SEC rules that permit “test the waters” activities already. However, unlike the existing “test the waters” provisions, the provisions of H.R. 3606 would not require companies to file with the SEC and take responsibility for the materials they use to solicit investor interest, even after they file for their IPOs. This would result in uneven information for investors who see both the “test the waters” materials and the prospectus compared to those who only see the prospectus. In addition, as with the provisions relating to research reports, it could result in investors focusing their attention on the “test the waters” materials instead of the prospectuses, without important investor protections being applied to those materials.

Confidential Filing of IPO Registration Statements

H.R. 3606 would permit emerging growth companies to submit their registration statements confidentially in draft form for SEC staff review. This reduction in transparency would hamper the staff's ability to provide effective reviews, since the staff benefits in its reviews from the perspectives and insights that the public provides on IPO filings. It also could require significant resources for staff review of offerings that companies are not willing to make public and then abandon before making a public filing. SEC staff recently limited the general practice of permitting foreign issuers to submit IPO registrations in nonpublic draft form because of these concerns, and expanding that program to all IPOs could adversely impact the IPO review program.

Crowdfunding

H.R. 3606 also provides an exemption from Securities Act registration for "crowdfunding," which would permit companies to offer and sell, in some cases, up to \$2 million of securities in publicly advertised offerings without preparing a registration statement. For the past several months, the staff has been analyzing crowdfunding, among other capital formation strategies, and also has discussed these strategies with the Commission's newly created Advisory Committee on Small and Emerging Companies.²

I recognize that proponents of crowdfunding believe this method of raising money could help small businesses harness the power of the internet and social media to raise small amounts of very early stage capital from a large number of investors. That said, I believe that the crowdfunding exemption included as part of H.R. 3606 needs additional safeguards to protect investors from those who may seek to engage in fraudulent activities. Without adequate protections, investor confidence in crowdfunding could be significantly undermined and would not achieve its goal of helping small businesses.

For example, an important safeguard that could be considered to better protect investors in crowdfunding offerings would be to provide for oversight of the industry professionals that intermediate and facilitate these offerings. With Commission oversight, these intermediaries could serve a critical gatekeeper function, running background checks, facilitating small businesses' provision of complete and adequate disclosures to investors, and providing the necessary support for these small businesses. Commission oversight would further enhance customer protections by requiring intermediaries to protect investors' and issuers' funds and

² That advisory committee, which includes executives, owners, investors and advisors of privately-held small businesses and smaller public companies, recently adopted several recommendations on capital formation, but declined to place a crowdfunding recommendation before its members for a vote, expressing concern regarding the usefulness of crowdfunding as a capital formation tool for small and emerging businesses and the potential significant investor protection concerns. In addition, certain Committee members involved in investing in small private companies worried that the impact on the capital structure of small companies resulting from a crowdfunding capital raise may have a detrimental effect on attracting subsequent and more meaningful rounds of financing.

securities, for example by requiring funds and securities to be held at an independent bank or broker-dealer.

Investors also would benefit from a requirement to provide certain basic information about companies seeking crowdfunding investors. H.R. 3606 requires only limited disclosures about the business investors are funding. Additional information that would benefit investors should include a description of the business or the business plan, financial information, a summary of the risks facing the business, a description of the voting rights and other rights of the stock being offered, and ongoing updates on the status of the business.

Changes to Section 12(g) Registration Thresholds

H.R. 3606 also would change the rules relating to the thresholds that trigger public reporting by, among other things, increasing the holder of record threshold that triggers public reporting for companies and bank holding companies. The current rules have been in place since 1964, and since that time there have been profound changes in the way shareholders hold their securities and in the capital markets.

Last spring, I asked our staff to comprehensively study a variety of capital formation-related issues, including the current thresholds for public reporting. At this point, I do not have sufficient data or information to assess whether the thresholds proposed in H.R. 3606 are appropriate. I do recognize that a different treatment may be appropriate for community banks that are already subject to an extensive reporting and regulatory regime.

Rulemaking

H.R. 3606 requires a series of new, significant Commission rulemakings with time limits that are not achievable. For example, the rulemaking for the crowdfunding section has a deadline of 180 days, and it specifically requires the Commission to consider the costs and benefits of the rules. Given (1) that much of the data that would be used to perform such analyses is not readily available and (2) the complexity of such analyses, this time frame is too short to develop proposed rules, perform the required analyses, solicit public comments, review and analyze the public comments, and adopt final rules. I believe a deadline of 18 months would be more appropriate for rules of this magnitude.

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The Honorable Richard C. Shelby
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I stand ready to assist Congress as it addresses these important issues. Please call me, at (202) 551-2100, or have your staff call Eric Spitzer, Director of the Office of Legislative and Intergovernmental Affairs, at (202) 551-2010, should you have any questions or comments.

Sincerely,



Mary L. Schapiro
Chairman