Signal Hill Capital

January 31, 2005

Ms. Barbara Z. Sweeney
Office of the Corporate Counsel
National Association of Securities Dealers
1735 K Street, N.W.
Washington, D.C. 20006-1500

Re: NASD Notice to Members 04-83
(pp. 995-999 inclusive)

Dear Ms. Sweeney:

We are writing in response to the above referenced Notice to Members (the "Notice") as an NASD member firm ("Member") to offer comments on whether the NASD should propose a new rule that would address certain conflicts of interest issues when Members provide fairness opinions on transactions that involve a change in corporate control (a "Transaction" or "Transactions"). Signal Hill Capital Group LLC ("SHCG") is a Member primarily engaged in the business of providing strategic and financial advice to its clients regarding mergers, acquisitions, divestitures, restructurings and corporate reorganizations. Our business routinely involves delivery of fairness opinions relating to Transactions.

As a general matter, SHCG does not object to a rule that would cause the identification and disclosure of any conflicts of interest that a Member might have when rendering a fairness opinion on a Transaction. However, SHCG does have some serious concerns about any rule mandating certain procedures regarding analytical process that a Member must follow and disclose as we do not believe that any one set of procedures can be described in a rule that would be flexible and dynamic enough to fit all circumstances. Lastly, SHCG has some equally serious concerns about (i) what information is disclosed regarding conflicts of interest and the procedures employed by a Member in analyzing Transactions and reaching an opinion of fairness and (ii) where such information is to be disclosed.

IDENTIFICATION AND DISCLOSURE OF CONFLICTS OF INTEREST

As referenced earlier, SHCG is in support of a new NASD rule that would identify and disclose to the Board of Directors, Management and, ultimately, the shareholders of a client company involved in a Transaction (the "Board," "Management," and "Shareholders," respectively) any "significant conflicts of interest" of a Member rendering a fairness opinion on the subject Transaction. While this is typically an issue

Signal Hill Capital Group LLC • 6225 Smith Avenue, Suite 202 • Baltimore, Maryland 21209-3630
Tel 443-796-4000 • Fax 443-796-4002 • www.signalhillcapital.com

resolved by the Board or a sub-committee of the Board during the adviser selection process, we believe any conflict of interest that arises with a Member should be disclosed. For the purpose of this discussion, we assume that a conflict of interest is a set of conditions, contracts or relationships relating to a Member that might affect the Member's ability to review, analyze, value and render an opinion as to the fairness of a Transaction objectively, without bias in favor of or against the subject Transaction. We would first note that the Securities and Exchange Commission ("SEC") rules and regulations do mandate disclosure of any "Material Relationship" in a proxy relating to a Transaction. These requirements are augmented by state securities disclosure requirements. Notwithstanding these requisite disclosures, should the NASD feel there is a need for such a rule, we would favor such a rule insofar as it causes the Member to disclose its role in the subject Transaction if such role involves more than rendering a fairness opinion. Such additional roles might include:

- any role in negotiating the terms of the Transaction on behalf of the client company;

- any role in providing, arranging or securing debt or equity financing for or in anticipation of the Transaction;

- other Investment Banking Services (as defined in NYSE Rule 472.20) performed for the company within a specified period preceding the delivery of the fairness opinion (the NASD should define the time period in an exposure draft of any rule issued for comment);[1] and

- any additional Investment Banking Services the Member might be awarded as a result of rendering the fairness opinion.

In addition we would believe it prudent to disclose the type of any fee payments due to a Member as a result of its role in a Transaction including:

- fees for delivery of the fairness opinion;

- fees due to the Member as a contingency upon the closing of the Transaction or closing of any financing provided, arranged or secured in anticipation or completion of the Transaction; and

- any other incentive fees due to the Member on account of the successful completion of the Transaction.

---

[1] NYSE Rule 472.20 provides that Investment Banking Services "...include, without limitation, acting as an underwriter in an offering by the [company], acting as a financial advisor in a merger or acquisition; providing venture capital, equity lines of credit, PIPES (private investment, public equity transaction), or similar investments; or serving as placement agent for the issuer."

In regard to disclosure of any of the foregoing, it is extremely important that any new rule clearly define "significant conflicts of interest" as described in the Notice, as it implies there may be an acceptable level of "insignificant conflicts of interest" to the NASD. In creating this definition, the NASD staff must carefully consider and differentiate among actual, potential and perceived conflicts of interest and their relative materiality. Once the resulting definition(s) are developed, they should be part of any final comment period allowed for the exposure draft of the new rule.

RELIANCE ON COMPANY DATA

Separately, the NASD has posed for comment in the Notice whether the new rule should address disclosure by a Member of its reliance on the company for key information related to the Member's analysis of and determination of fairness of a Transaction. SHCG believes these disclosures (at least in the experience of its bankers) are already provided in most opinion letters as a standard practice and does not need to be addressed.

SHCG believes that there is an unavoidable conflict of interest in a Member's reliance on Management or the company for information related to a Transaction, which is why inclusion of exculpatory language in opinion letters is standard practice by Members. In particular, while audited historical information can be provided on a reasonably objective basis, that data only forms a part of the input in the analysis and valuation of a company and the resulting terms of a Transaction. Usually, there is a greater emphasis placed on the prospects of a company's business or the combined companies' businesses as a result of a Transaction and the resulting financial projections. The only data available to a Member for this portion of its analysis and valuation is projections generated by Management that are usually a result of a planning process, which projections are usually approved by the Board, or discussions and projections of the buyer's and target's management teams throughout the negotiation of a Transaction.

In analyzing a company or the companies involved in a Transaction, a Member must rely on Management of its client company not only for projections but also for its views of and best judgments (as well as those of Management for the counter-party company) on:

- prospects and projections of the acquirer and the target,
- projections of any expense savings and economies resulting from a combination and how that might change with different parties to a Transaction;
- projections of estimated revenue enhancements, cost savings, or shutdown costs.

It is inappropriate for Members to fabricate what they think financial projections will be which is why an appropriate due diligence inquiry with management of both companies involved in a Transaction is also industry practice. A Member must temper its views of the data and projections provided by performing due diligence and interviewing managements to assess the reasonability and achievability of assumptions underlying the projections and what makes them sensitive and susceptible to change. From that review, the Member customarily develops its own view of the prospects and projections resulting from the Transaction. Members customarily perform sensitivity analyses on the projections to assess what might happen to the financial projections under varying scenarios. However, in order to perform these analyses, Members have no choice but to rely on managements and the companies involved for the prospective information and, for that reason, there already is a standard practice of disclosing this reliance in the fairness opinion letter itself.

INDEPENDENT VERIFICATION OF INFORMATION BY MEMBERS

As to the NASD's possible inclusion in the new rule of disclosure by a Member issuing a fairness opinion of procedures regarding the independent verification of certain company supplied information, that too is already addressed as a standard practice in fairness opinion letters. The standard practice language states that the data received has not been independently verified and usually continues to say that no appraisal was performed by the Member as to the value of the company's assets. Members are not auditing or appraisal firms. They are not contracted to and they do not undertake to audit or verify financial statements or projections. Instead, Members rely on the company's (in many cases, companies') representations and the auditor's (or auditors') opinion and "comfort" letters as to historical data, and conduct Management interviews as noted above to obtain comfort as to the prospective data.

Finally, as to whether a Member has received from Management or the Board any specific instructions, limitations, assumptions or constraints within which to limit its work or opinion, those are also, as standard practice, stated in the fairness opinion as part of the assumptions and limitations of a Member's work. Therefore, we do not believe any new rule needs to address this issue.

MANDATING SPECIFIC PROCEDURES TO GUARD AGAINST CONFLICTS OF INTEREST

As stated in our introduction, SHCG is not in favor of the NASD mandating in a new rule a set of specific procedures for Members to follow when rendering fairness opinions. In making our comments, we presume the goal of any new NASD rule on this issue is to provide more information to shareholders. First, it is not clear that any one set of procedures would be appropriate for all types of Transactions – mergers, acquisitions, sales, divestitures, joint ventures, as well as others - and the different terms that accompany each.

Second, SHCG does not believe that a rule can or should address the "substantive factors used by [M]embers in reaching a fairness opinion" and the disclosure of same. The analysis and valuation work performed by a Member in providing a fairness opinion varies greatly and depends on, among other things, the companies involved in a Transaction, how the public and private markets value those companies and industries, the structure of the Transaction itself including different terms and conditions, valuation factors unique to the companies involved and the process Management and the Board employed to pursue a Transaction. Therefore, promulgation of a set of specific procedures or factors is unlikely to be universally effective. The alternative is that any such procedures or factors will be too general to provide useful direction to the Member or useful disclosure to shareholders.

In addition, to the extent the NASD is looking to mandate disclosure about the salient factors considered by a Member in reaching the decision that a transaction is fair, the staff should consider that for companies that are publicly traded and must seek shareholder approval for a Transaction, proxy disclosure rules regarding issuers of securities (the companies) are already in effect under SEC regulations. These regulations compel an issuer to disclose a great deal of information for shareholders in a proxy statement related to a Transaction, including the report and letter of the Member providing the fairness opinion to the Board. We would also note that over the last decade the SEC has been requiring greater levels of detail in proxy statement disclosure as to a Member's valuation procedures and comparative analysis in rendering a fairness opinion. It appears that the disclosure standards today are almost uniformly equal to the detailed disclosure standards that are required in Transactions subject to Section 13(e) of the Securities Exchange Act of 1934.[2] In our view, adding any of this type of disclosure to the fairness opinion letter itself would duplicate what is already in the proxy and render the opinion letter itself lengthy and turgid, possibly to the point of obscuring the primary points of the opinion letter, that, in the Member's view, as expressed to the Board, the Transaction is fair from a financial point of view to the shareholders taken as a whole.

Another item the NASD has suggested for consideration in the Notice is that the Member should, by disclosing the Member's internal procedures used by its Fairness

---

[2] It is SHCG's view that the current SEC disclosure requirements for inclusion in the proxy statement of publicly traded companies involved in a Transaction are appropriate and thorough. To the extent the NASD feels it is necessary, SHCG would not object to similar disclosure requirements on behalf of the shareholders of non-publicly traded companies involved in a Transaction, but only to the extent the company or its Board has received a fairness opinion and related materials, or instances where the Board of a publicly traded company receives a fairness opinion on a Transaction but the company would not disclose the particulars of the Transaction or the fairness opinion to its shareholders because a shareholder vote is not required. In both types of situations, the Board may become the primary beneficiary of the disclosure of the factors in a Member's determination of fairness of a Transaction. This may or may not affect the outcomes of directors' votes on Transactions in the future were this to occur. The shareholders would obviously also benefit from the disclosure of such information in deciding how to vote their shares, were that required.

Opinion Committee, confirm that there are no conflicts of interest in the composition of or process used by the Fairness Opinion Committee. SHCG does not object to disclosure about the existence of such a committee and the disinterested status of its members for the subject Transaction. However, we strongly disagree with any disclosure as to the committee's process or deliberations. First, the financial audit community does not disclose the interested or disinterested relationships of the members of the peer review committee or its peer review process and deliberations for issuing opinions on financial statements. These are publicly available statements made available to shareholders annually and there is no disclosure requirement for auditors. We do not believe Members should be held to a higher standard for one time reports when the auditors are not held to similar standard for annual reports. Second, adding additional disclosure on this topic would not be helpful for shareholders as the relevant data and considerations are already disclosed in the proxy descriptions. This would be redundant with material already made available.

MANAGEMENT AND BOARD COMPENSATION IN A TRANSACTION

SHCG does not believe it is in the purview of a Member retained to render a view as to the fairness of a Transaction to comment extensively on compensation matters. First, Members are generally not compensation experts and are not in the business of issuing reports on compensation matters. Second, most compensation payments triggered by a Transaction are put in place long before the Transaction is even contemplated. These pre-existing compensation contracts are agreed to by the Board with the thorough review of the Compensation Committee which is usually assisted by outside compensation experts. The Board owes a fiduciary obligation to its shareholders and is in the best position to determine what compensation should be paid to Management in the event of a Transaction.

Finally, Members are customarily retained and contracted to render an opinion of the fairness of the proposed Transaction from a financial point of view to the shareholders taken as a whole. Members traditionally do not opine on the breakdown of value among shareholders or other interested parties. In many cases, due to compensation contracts already in place as stated above, there is little impact that a Member or a Transaction can have on Management compensation other than triggering a payment event. Further, Members do not customarily review compensation matters unless in extreme situations, employment contracts and stock incentive plans deduct from consideration otherwise due to shareholders. Even in those instances, it would not be appropriate for a Member to retain an outside compensation expert to review the terms of Management's or directors' compensation. That would properly be the purview of the Board or the Compensation Committee. For a Member to comment on a matter that it was not retained to review and in which it is not expert would be unprofessional conduct and improper. Rather, the NASD should consider whether Regulation S-K, Items 402 and 404, are adequate to compel disclosure of such compensation matters and whether such compensation disclosure may be properly added at the request of the SEC examiner

reviewing the proxy. If necessary, such disclosures should be made in the proxy complete with any expert compensation reports received by the Compensation Committee or Board regarding the propriety of the compensation plans and/or compensation levels including any change in control provisions.

LOCATION OF ANY ADDITIONAL DISCLOSURE

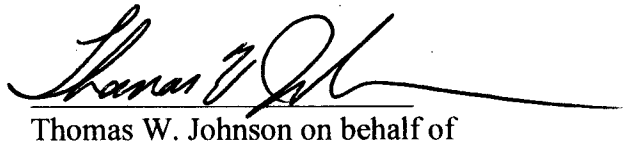
To the extent new disclosure rules are enacted, serious consideration should be given by the staff of the NASD as to where any additional information to be disclosed should appear. We respectfully submit that there should not be new disclosure rules regarding the content of fairness opinion letters. A fairness opinion letter is drafted for, and is to be relied upon solely by, the Board. It has been contracted for by the Board and the fairness opinion is delivered exclusively to it for its benefit. The Board, or a sub-committee of the Board, has interviewed candidate Members to deliver the fairness opinion and the Board or sub-committee customarily vets credentials, including but not limited to industry expertise, Member firm capabilities and possible conflicts of interest. Further, to the extent any new NASD disclosure rules that are the subject of the Notice apply for the benefit of shareholders, those new disclosures should appear in the proxy statement disclosures which are provided especially for the benefit of shareholders and which disclosures are carefully monitored, reviewed and commented upon by the SEC. This is where shareholders now look to find detailed disclosures about the Transaction in question, including the fairness opinion particulars. Further, to the extent a Member feels any additional disclosures that are the subject of the Notice and are made in a Proxy statement need to be included in its fairness opinion documents, the decision as to whether to put those disclosures in the fairness opinion letter itself or any supporting materials should be left to the discretion of the Member. The Member should determine where this information should be disclosed in the reports it delivers to its Board client.

CONSISTENCY OF DISCLOSURE RULES

SHCG respectfully submits that any new rules the NASD considers regarding additional disclosure of a Member's role in providing a fairness opinion on a Transaction should be drafted with a view to being consistent with SEC proxy disclosure rules and regulations already in place for issuers of securities. Much of what the NASD seeks to address is already encompassed within the authority of the SEC.

We thank you for the opportunity to comment on the Notice. We would be happy to discuss our views on any of the foregoing with the NASD.

Sincerely,



Thomas W. Johnson on behalf of
Signal Hill Capital Group LLC