provides an acceptable level of safety may be used if approved by the Manager, Rotorcraft Standards Staff, Rotorcraft Directorate, FAA. Operators shall submit their requests through an FAA Principal Maintenance Inspector, who may concur or comment and then send it to the Manager, Rotorcraft Standards Staff.

Note 2: Information concerning the existence of approved alternative methods of compliance with this AD, if any, may be obtained from the Rotorcraft Standards Staff.

(d) Special flight permits may be issued in accordance with sections 21.197 and 21.199 of the Federal Aviation Regulations (14 CFR 21.197 and 21.199) to operate the helicopter to a location where the requirements of this AD can be accomplished.

Note 3: The subject of this AD is addressed in Direction Generale De L'Aviation Civile (France) AD 96–173–077(B)R1, dated April 23, 1996.

Issued in Fort Worth, Texas, on February 26, 1998.

Eric Bries,

Acting Manager, Rotorcraft Directorate, Aircraft Certification Service.

[FR Doc. 98–5734 Filed 3–4–98; 8:45 am]

BILLING CODE 4910–13–U

DEPARTMENT OF COMMERCE

National Oceanic And Atmospheric Administration

15 CFR Part 960

Licensing of Private Remote-Sensing Space Systems

AGENCY: National Oceanic And Atmospheric Administration, Department of Commerce.

ACTION: Notice of public Hearing.

SUMMARY: On November 3, 1997, the National Oceanic And Atmospheric Administration (NOAA) proposed regulations revising its regime for the licensing of private remote sensing space systems under Title II of the Land Remote Sensing Policy Act of 1992, 15 U.S.C. 5601 *et seq*. (1992 Act) (62 FR 59317). As part of this rulemaking, NOAA is sponsoring a public meeting to solicit comments from the public on the proposed rule.

DATES: The Public Meeting will be held on April 1, 1998, from 8 a.m. to 5 p.m., with a lunch break from 12 p.m. to 1 p.m.

ADDRESSES: The meeting will be held at the United States Department of Commerce, Herbert C. Hoover Building, Room 4830, 14th Street & Constitution Avenue, NW, Washington, DC. Parties interested in participating in the public meeting, particularly those that would like to present oral and/or written testimony, should contact Charles Wooldridge or Kira Alvarez (See **FOR FURTHER INFORMATION CONTACT**) by March 27, 1998. Comments received to date in response to the notice of proposed rulemaking (NPRM) may be viewed and/or copied by appointment from 9 a.m. to 3 p.m. at NOAA, National Environmental Satellite, Data and Information Service, 1315 East West Highway, Rm 3620 Silver Spring, Maryland.

FOR FURTHER INFORMATION CONTACT: Charles Wooldridge, NOAA, National Environmental Satellite, Data, and Information Service, (301) 713–2024 x 107 or Kira Alvarez, NOAA, Office of General Counsel, (301) 713–1329.

SUPPLEMENTARY INFORMATION: On November 3, 1997, NOAA published a Notice of Proposed Rulemaking (62 FR 59317) proposing regulations revising its regime for the licensing of private Earth remote-sensing space systems under Title II of the Land Remote Sensing Policy Act of 1992, 15 U.S.C. 5601 *et seq*. (1992 Act). These proposed regulations implement the licensing provisions of the 1992 Act and the Presidential Policy on remote sensing announced March 10, 1994. NOAA is sponsoring this public meeting to solicit comments on the proposed rule.

Parties are encouraged to bring a copy of their proposed oral testimony. Due to time constraints, NOAA may have to limit the length of oral statements on some of the topics. The proposed agenda is as follows:

8:00–8:30 Registration and Coffee
8:30–9:00 Welcome and Introduction
9:00–10:00 General
- § 960.1 Purpose
- § 960.2 Scope
- § 960.3 Definitions

10:15–12:00 Procedures
- § 960.4 Pre-application Consultation
- § 960.5 Filing Information
- § 960.6 Information to be included in an Application
- § 960.7 Confidentiality of Information
- § 960.8 Review Procedures for License Applications
- § 960.13 Amendment to Licenses

12:00–1:00 Lunch
1:00–4:00 National Security, Foreign Policy and Investment Agreements
- § 960.9 Conditions for Operations [subsections (b), (c), (g)]
- § 960.10 National Security, International Obligations, and Foreign Policy
- § 960.12 Notification of Foreign Agreements
- § 960.14 Investment Agreements

4:00–5:00 Other
- § 960.9 Conditions for Operations [subsections (a), (d) (e), (f), (h), (i)]
- § 960.11 Data Policy
- § 960.15 Certain Rights not Conferred
- § 960–16–20 Enforcement Procedures

5:00 Closing Remarks

Dated: March 2, 1998.

Robert S. Winokur,

Assistant Administrator for Satellite and Information Services.

[FR Doc. 98–5744 Filed 3–4–98; 8:45 am]

BILLING CODE 3510–12–M

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 230

[Release No. 33–7511; File No. S7–5–98]

RIN 3235–AG21

Rule 701—Exempt Offerings Pursuant to Compensatory Arrangements

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The current dollar limitations on the amount of securities that may be offered and sold under the Commission's Rule 701 under Securities Act of 1933 which provides an exemption from registration for such securities pursuant to compensatory benefit arrangements may be too restrictive. Therefore, we propose to amend these limitations to permit companies greater access to the exemption if certain disclosure requirements are satisfied.

DATES: Public comments should be received on or before May 4, 1998.

ADDRESSES: Please send three copies of the comment letter to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. You can send comments electronically to the following e-mail address: rule-comments@sec.gov. The comment letter should refer to File No. S7–5–98; if e-mail is used please include the file number in the subject line. Anyone can inspect and copy the comment letters at our Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549. We will post comment letters submitted electronically on our Internet site (http://www.sec.gov).

FOR FURTHER INFORMATION CONTACT: Richard K. Wulff (202–942–2950), Office of Small Business, Division of Corporation Finance, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION:

I. Executive Summary

Rule 701[1] under the Securities Act of 1933 (''Securities Act'')[2] was adopted in 1988 to allow private companies to sell securities to their employees without the need to file a registration statement in the same manner as a public company. At that time we determined that it would be an unreasonable burden for these private companies, many of which are small businesses, to incur the expenses and disclosure obligations of public companies when their only public sales were to employees. This is especially true because these sales were for compensatory and incentive purposes, rather than capital-raising. To accommodate these companies, we used the maximum extent of our exemptive authority and exempted offers and sales of up to $5 million per year.

Over the years, the Commission staff monitored the use of the rule. Until mid-1993, Form 701 was required to be filed with us whenever an offering under the rule was made. On the basis of that data and feedback from practitioners, the staff has concluded that the rule has been popular for both small businesses and larger private companies (such as mutual insurance companies, foreign issuers, and engineering firms), but that the $5 million limit has been particularly restrictive in light of: the popularity of equity ownership by employees; inflation; and the growth of deferred compensation plans (which are eligible for the rule). In addition, the staff has concluded that the rule needs further simplification and clarification.

In October 1996, Congress enacted the National Securities Markets Improvement Act of 1996 (''NSMIA'')[3] which, for the first time, gave us the authority to provide exemptive relief beyond $5 million for transactions such as these. The legislative history of NSMIA suggested specifically that the $5 million ceiling on Rule 701 be lifted.[4] As detailed below, we propose today to modify the ceilings and to further simplify and streamline the rule. To ensure continued investor protection along with the added flexibility, we propose to mandate that a company must give any purchaser specific types of disclosure.

We seek to increase the flexibility and utility of Rule 701 by issuing proposals that would:

(1) Remove the artificial $5 million ceiling and instead set the maximum amount of securities that may be sold in a year at the greatest of:
$1 million;
15% of the issuer's total assets; and
15% of the outstanding securities of that class

(2) Not count offers for purposes of calculating the ceiling;

(3) Require the issuer to disclose certain risk factors that may be associated with investment in securities pursuant to the plan or agreement, and deliver financial statements in accordance with Form 1–A of Regulation A[5] to each person to whom securities are sold;

(4) Amend Rule 701 to comport with current and more flexible interpretations; and

(5) Simplify the Rule.

Together, these changes will add greater flexibility for companies to sell securities to their employees and, at the same time, will provide that essential information be delivered to employees in a timely manner.

II. Background

Rule 701 was adopted under section 3(b) of the Securities Act to provide an exemption from the registration requirements of that Act for offers and sales of securities pursuant to certain compensatory benefit plans or written agreements relating to compensation.[6] The exemptive scope covers securities offered or sold pursuant to a plan or agreement established by a non-reporting (''private'') company, its parents or majority-owned subsidiaries, to their employees, directors, partners, trustees, consultants and advisors.

Currently the rule provides that the amount of securities that may be subject to outstanding offers in reliance on Rule 701 plus the amount of securities offered or sold under the rule in the preceding 12 months may not exceed the greater of $500,000, or an amount determined under one of two different formulas. One formula limits the amount to 15% of the issuer's total assets measured at the end of the issuer's last fiscal year. The other formula restricts the amount to no more than 15% of the outstanding securities of the class being offered. Regardless of the measurement method elected, the Rule restricts the aggregate offering price of securities subject to outstanding offers and sold in the preceding 12 months to no more than $5 million.

A. Concerns With the Current Rule

In the decade since adoption of Rule 701, equity ownership by employees has grown exponentially. Not only have employees benefited generally as the value of their stock has appreciated, but companies' managements have widely encouraged equity participation as a retention and incentive device for employees. In addition, companies have sought to provide tax benefits and possible investment opportunities by offering many of their senior and middle management personnel participation in deferred compensation plans. To the extent these plans involve an offer of securities, they are eligible to use Rule 701. The growth of these plans, coupled with the impact of inflation, has caused the $5 million annual limit to be impractical for many companies.

In addition to concerns with the ceiling, a myriad of interpretive questions have arisen under the current rule. While every new rule needs routine interpretive gloss from the Commission staff, Rule 701 has been the subject of an abundance of highly technical requests for clarification. Some of these issues include how to treat stock options, former employees, subsidiaries, consultants, advisors, and successor issuers, and when to integrate Rule 701 offerings with other exempt offerings under the federal securities laws. In summary, the rule needs to be both simplified and modernized.

B. National Securities Markets Improvement Act of 1996

In October 1996, NSMIA was signed into law. Title I of that statute relating to ''Capital Markets'' adds section 28 to the Securities Act providing us with general exemptive authority from any provision of the Securities Act.[7] During the legislative process, both the House Committee on Commerce[8] and the Senate Committee on Banking, Housing and Urban Affairs[9] noted, in

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[1] 17 CFR 230.701.

[2] 15 U.S.C. 77a *et seq.*

[3] Pub. L. 104–290, 110 Stat. 3416 (October 11, 1996).

[4] Both Committee Reports specifically highlighted the current $5 million limit contained in Rule 701 and seek prompt Commission action to raise that ceiling. H.R. Rep. No. 104–622 at 38; S. Rep. No. 104–293 at 16.

[5] 17 CFR 230.251–263.

[6] Release No. 33–6768 (April 14, 1988) [53 FR 12918].

[7] The Commission, by rule or regulation, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation issued under this title, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors. 15 U.S.C. 77bb. New section 2(b) of the Securities Act requires that when we engage in rulemaking and are required to consider the public interest as well as the protection of investors, we also must consider ''whether the action will promote efficiency, competition, and capital formation.''15 U.S.C. 77b(b).

[8] H.R. Rep. No. 104–622 (June 17, 1996) at 38.

[9] S.Rep. No. 104–293 (June 26, 1996) at 15–16.

considering this provision, that we should take steps to increase the ceilings in our existing exemptions promulgated under section 3(b) of the Securities Act. The legislative history of NSMIA reflects a specific Congressional concern about the current $5 million aggregate offering price ceiling in Rule 701 having a negative impact for many issuers of securities in compensatory arrangements.

III. Proposed Amendments to Rule 701

A. Exemptive Limits

The current rule limits the dollar amount of securities *offered* to employees, regardless of how many securities are *sold* to employees. Calculations based on offers for this purpose are problematic, especially in determining how to treat options, warrants, rights and other exercisable or convertible securities (which represent offers to sell the underlying securities). In light of our new exemptive authority, we propose eliminating the restriction in the dollar amount of securities that may be *offered* pursuant to the rule since limiting the amount of offers is not necessary to assure that these transactions are not so large as to necessitate registration. Instead, a test that focuses on the amount of sales in each 12-month period should serve that purpose.

Changing the focus to sales means that issuers no longer will have to calculate and regularly monitor the amount of options, warrants, rights or other exercisable or convertible securities, but rather can focus solely on the amount of securities sold. This change also reduces the likelihood that companies will restrict eligibility or participation in a compensatory benefit plan solely to meet an offering limit. This proposal would make the exemption more usable to a greater number of companies, including those that maintain deferred compensation plans, but are not reporting companies under the Exchange Act and therefore do not qualify to utilize Form S–8.[10] Commenters are asked to address whether removing offers from the calculation is appropriate or whether we should limit the amount of securities being offered as well as, or instead of, a limit on the amount of securities sold.

As part of eliminating the ceiling on the amount of offers of securities that may be made pursuant to the rule, we propose eliminating outstanding offers from the calculation under the two formulas for determining the aggregate sales price or number of securities that may be sold in a 12-month period. By only measuring the amount of securities sold against the 15% of assets formula or the 15% of outstanding securities formula, some issuers will be given more flexibility and an increase in the limit on the amount of securities that they may sell. The proposal also will greatly simplify a highly technical calculation and the resulting need for incremental interpretation. We believe no investor protection concerns are presented by this added flexibility, but solicit comment as to whether there might be unanticipated abuses.

Rule 701 has become increasingly of limited utility to larger companies due to the $5 million limitation. We believe that this would be the case even if we re-focus the limitation on sales. Moreover, the more appropriate focus is not the absolute dollar amount sold, but rather how the amount compares to the size of the company and its capital base. Therefore, we propose to eliminate the $5 million aggregate offering price ceiling and rely on the three-part calculation of the amount of securities that may be sold in a 12-month period to set a more appropriate dollar limit. In addition, we propose to amend Rule 701 so that the issuer's most recent balance sheet date would be used for purposes of that calculation. This would make the measurement consistent and avoid confusion as to the date to be used when performing the calculation.[11] Comment is solicited as to whether a specific aggregate offering price ceiling, such as $10 million, $15 million or $20 million, is preferable to no ceiling, and whether we should change the measurement periods as we propose. We also solicit comment as to whether non-reporting foreign issuers should be subject to an annual limit, such as $10 million, because the application of the calculation to large foreign private companies could result in the sale of a large amount of securities to a large number of employees without such companies ever being required to register under either the Securities Act or the Exchange Act.[12]

Comment is solicited as to whether Rule 12g3–2(b) should be amended so that foreign private issuers that either sell securities under Rule 701 or sell more than some annual threshold amount under the rule, such as $10 million, would be ineligible for the Rule 12g3–2(b) exemption since that exemptive relief from reporting under Section 12(g) is predicated on the foreign issuer not taking any steps to enter the U.S. market voluntarily.

It is not only the $5 million ceiling that has an obvious limiting effect; the $500,000 level used in the calculation also has such an effect. We are particularly concerned that many small businesses are unnecessarily constrained by this limit. We therefore propose setting this level of the amount of securities sold in reliance on the rule during a 12-month period at $1 million. The proposed $1 million limit should ensure issuers adequate flexibility. Thus, regardless of total assets or outstanding securities, a private company could always sell up to $1 million in securities to its employees in a 12-month period. We note that this level would be consistent with the $1 million offering exemption in Rule 504 of Regulation D.[13] (Unlike Rule 504, however, securities sold under Rule 701 are ''restricted'' securities and cannot be freely resold.) We request comment on whether the alternative level allowed under Rule 701 should be limited to $1 million, as proposed, or alternatively whether the amount should be retained at $500,000 or raised to $750,000, $1.5 million or $2 million.

We propose that the changes in the Rule 701 ceilings would apply to plans and agreements currently covered by the rule, including those with consultants and advisors. We do not propose to change the status of securities sold under the rule, so that the securities would continue to be ''restricted'' and subject to resale restrictions. We do not anticipate that the same types of abuses that are associated with Form S–8, with issuers selling securities to consultants and advisors, who are in effect underwriters in reselling the securities to the public, would arise because the securities would be restricted. However, we solicit comment as to whether Rule 701 should retain consultants and advisors as eligible participants pursuant to the rule, whether the current offer and sale ceilings should be retained for consultants and advisors, and whether the definition of consultant

[10] 17 CFR 239.16b. Form S–8 is a simplified form for registering securities for sale to employees but is limited to public companies which file reports pursuant to the reporting requirements of the Exchange Act.

[11] Under the current rule, assets are calculated as of the end of its last fiscal year. The rule is silent as to when outstanding securities are calculated.

[12] Domestic issuers that acquire more than 500 shareholders and have assets exceeding $10 million must register under Section 12(g) of the Exchange Act. Foreign private issuers crossing those thresholds may instead rely on the exemption from Section 12(g) provided by Rule 12g3–2(b). 17 CFR 240.12g3–2(b). The rule exempts from Exchange Act registration securities of a foreign private issuer if the issuer furnishes to us annual and other reports and other materials that are publicly available in its home market.

[13] 17 CFR 230.504.

and advisor should be narrowed to the definition used with Form S–8.

B. Disclosure to Persons Covered by Rule 701

Similar to some private placements, there is no requirement in Rule 701 to deliver a specific disclosure document to buyers other than a copy of the relevant compensation plan or agreement. However, because these transactions are subject to the antifraud provisions of the federal securities laws,[14] we understand that many companies prepare an offering document to provide information to employee investors.[15] While we are not aware of any widespread abuses, we are concerned that the increased flexibility added by today's proposals could lead to a series of larger transactions and consequently a broader impact on U.S. investors. While it may be burdensome to impose specific disclosure requirements on small transactions by small businesses, the cost-benefit balance may shift because the amended rule would facilitate larger transactions to potentially unsophisticated employees.

We propose that sales of securities under Rule 701 would require that the employees and other persons covered by the rule be supplied with recent financial and other information a reasonable period of time prior to the sale of such securities. We propose that this disclosure include the risk factors associated with investment in the securities pursuant to the plan or agreement and the financial statements required in an offering statement pursuant to Form 1–A of Regulation A under the Securities Act.[16] Regulation A allows for simpler unaudited financial statements. We also propose that the financial statements be as of a date no more than 180 days prior to the sale of such securities.[17]

We do not believe that this limited disclosure would be unduly burdensome to private companies. In proposing such requirements, we note that issuers with deferred compensation plans would be required to disclose the material risks that may be associated with such plans, such as the risks arising from the unsecured nature of the companies' obligations.

Commenters are asked to address whether any specific disclosure requirements should be adopted. In this regard, commenters may want to address any differences between a disclosure regime for compensatory purposes and one for capital-raising purposes. Comment also solicited comment as to whether additional disclosure, such as the other requirements of Form 1–A, should be required. Commenters should address whether these disclosure requirements should apply to all Rule 701 sales, or only to those sales that exceed a specified minimum amount per 12-month period, such as $1 million. That approach would harmonize Rule 701 with Rule 504.

C. Other Disclosure Approaches

We considered information requirements other than Regulation A, such as those reflected in Rule 502 of Regulation D.[18] We decided however, not to use the Rule 502 requirements because, among other things, they require audited financial statements and more non-financial information. They would therefore be more burdensome on these companies, many of which are small businesses. At the same time, it does not appear that this level of information should be necessary for all persons participating in compensatory benefit plans. We also considered requiring the information requirements of Form SB–1, [19] which allows small business issuers to offer and sell up to $10 million worth of securities in any 12-month period under a Regulation-A-type format, and Form SB–2 [20] which uses the simplified Regulation S–B [21] rules. However, both of those forms also require audited financial statements as well as more non-financial information than what we propose. We request comment as to whether other informational requirements should be utilized rather than the proposed risk factor and financial, such as those in Rule 502, Form SB–1 or Form SB–2.

As an alternative, should the level of disclosure to employees depend on their level of sophistication? For example, executive officers (as defined by Rule 3b–7 under the Exchange Act), directors and general partners are very knowledgeable about the company/partnership and may not benefit significantly from a mandated disclosure document. ''Officers'' as defined by Rule 3b–2 can be presumed to be somewhat knowledgeable about the company but may have less access to company information than executive officers. For this group, the proposed financial statements and risk factor disclosure may be appropriate. For more junior employees, former employees, consultants, advisors, disclosure substantially similar to Form 1–A may be appropriate.[22] Would this approach be practical and better protect those employees who may not have the requisite knowledge about the company?

D. Plain-English Technical and Clarifying Revisions

We also propose to recast Rule 701 by making various non-substantive technical and clarifying revisions in plain English to make it more concise, readable and understandable. In this regard, we propose changes to make it clear that an issuer may combine several different exemptions under the Securities Act (such as Rule 701 and Rule 506 [23]), and that Rule 701 is available to plans and agreements encompassing consultants and advisors that are natural persons without regard to exclusivity of representation of the issuer, as long as they render *bona fide* services that are not in connection with capital-raising. Comment is solicited on to whether there should be other changes to make the rule more understandable. Comment also is solicited as to whether the proposed modifications would be helpful.

E. Other Interpretive Revisions

We would amend the rule in several ways to address a variety of questions that have arisen since its adoption.[24] This section describes each of these proposed changes.

1. Treatment of Affiliates

In the past few years, it has become increasingly commonplace to sell stock of a private subsidiary to employees of

[14] *See* 15 U.S.C. 77q(a) and 15 U.S.C. 78j(b).

[15] Issuers are reminded of the preliminary note to Rule 701 which reaffirms the obligations of issuers and persons acting on their behalf to provide disclosure to employees or other persons within the scope of the rule adequate to satisfy the antifraud provisions of the federal securities laws.

[16] Form 1–A [17 CFR 239.90] under Regulation A sets forth the financial and non-financial information required in an offering statement.

[17] Proposed Rule 701(g) would provide that the disclosure delivery obligation would apply a reasonable period of time prior to the date of sale, but not necessarily at the time offers are first made. For example, for stock options, disclosure would be required a reasonable period of time prior to the date of exercise, rather than at the time of grant or when the option becomes exercisable, and deferred compensation plans would have a disclosure delivery obligation a reasonable period of time prior to the date the employee makes the irrevocable election to defer.

[18] 17 CFR 230.502.

[19] 17 CFR 239.9.

[20] 17 CFR 239.10.

[21] 17 CFR 228.10 *et seq.*

[22] If this regime were adopted, the private nature of these companies may justify less disclosure about executive compensation than you would expect from a public company.

[23] 17 CFR 230.506.

[24] Not all staff interpretations need specific changes in Rule 701. For example, although the ability to make offerings to employees through a trust is not specifically stated in the rule, the staff has interpreted the rule to allow for such offerings.

a parent or affiliate subsidiary. Given that these transactions appear to retain the envisioned compensatory aspect, the proposed amendments would expand coverage to sales to employees of majority-owned subsidiaries of the issuer's parent (i.e., brother-sister subsidiaries).

We also understand that some subsidiaries, particularly those intending to use the rule for deferred compensation arrangements, may not be able to utilize to great effect the two formulas in the calculation of the maximum sales per 12-month period. They may not have sufficient assets or independent business operations to make the ''15% of assets'' formula meaningful or enough securities to make the ''15% of outstanding securities'' formula meaningful. Therefore, we propose to provide that if a parent (whether or not a reporting company) of a wholly-owned subsidiary fully and unconditionally guarantees the obligations of the subsidiary, and if such guarantee does not exceed 15% of the parent's assets, the subsidiary can use the 15% of assets formula with respect to its parent. In that situation, the parent would deliver its financial statements to satisfy the disclosure obligations.[25] Comment is requested as to whether employees of related companies would be sufficiently informed about their affiliates such that the information provided would suffice to protect them?

2. Treatment of Former Employees, Advisors and Consultants

The proposed amendments also would clarify an interpretive question relating to former employees by specifying that sales may be made to former employees under the rule. A condition to this treatment would be that at the time the offer of those securities was originally made the employee must have been a current employee. Comment is solicited as to whether companies similarly should be allowed to use the rule to sell securities to former directors, consultants and advisors.

Historically, the staff has interpreted broadly the definition of ''employee'' and ''consultant'' for purposes of Rule 701.[26] This interpretation does not appear to have resulted in any significant abuses. However, comment is solicited as to whether consultants and advisors should be restricted from using Rule 701 if they are directly or indirectly promoting the company's securities. Comment also is solicited as to whether sales to consultants and advisors who sell the company's products or services should be limited to those who derive a certain minimum percentage of their income from sales on behalf of the issuer, such as 20 percent.

3. Valuation of Services

The proposed amendments also would simplify the determination of value of consultant services for purposes of calculating aggregate sales limit. Rather than retaining different rules for employees and consultants, such as currently not counting employee services while counting consultants' and advisors' services, proposed Rule 701 would treat employee services the same as consultant/advisor services so that in both cases they would count for determining aggregate sales.

4. Transfers to Family Members

As senior and mid-management personnel receive an increasing proportion of their compensation in the form of securities, these investments assume greater significance in the context of estate planning transactions and other intra-family transfers, such as property settlements in connection with divorce. Given the common economic interest of family members evidenced by estate planning transactions and the non-capital raising nature of these transactions, we believe that Rule 701 should be available for sales to family donees of such securities and transferees who receive these securities in divorce proceedings. Therefore, we propose to amend Rule 701 so that it is available for immediate family members who have acquired such securities through a gift or a domestic relations order. For this purpose ''immediate family'' would be defined as in Form S–8 to include any child, stepchild, grandchild, parent, stepparent, grandparent, spouse, siblings, aunt, uncle, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law or sister-in-law, including adoptive relationships, trusts for the exclusive benefit of these persons, and other entities owned solely by these persons. This proposal would be consistent with the treatment of transferable securities pursuant to the pending proposals for Form S–8.[27]

5. Form 701

Should Form 701, a notice filing required to be filed when Rule 701 was first adopted, be reinstituted completely or substantially? How would this type of information be useful to investors? Should the form, if reinstituted, be required to be filed electronically on EDGAR? Should we require that copies of any consultant or advisor agreements be filed along with or described in Form 701? Would public disclosure help ensure that only *bona fide* consultants and advisors purchase securities from the company under the Rule?

IV. General Request for Comment

Any interested person wishing to submit written comments on the proposed rule amendments or suggest additional changes or comments on other matters that might have an impact on the proposals set forth in this release are invited to do so by submitting them in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. We request comment as to the impact of the proposals from the point of view of the public, as well as the entities required to make available information to persons covered by Rule 701. We will consider comments on this inquiry in complying with our responsibilities under section 19(a) of the Securities Act.[28] We further request comment on any competitive burdens that may result from adoption of the proposals. We will consider comments on this inquiry in complying with our responsibilities under section 23(a) of the Exchange Act.[29] Comment letters should refer to File No. S7–5–98. All comments received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549.

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[25] Rule 701 would provide that, in limited situations, the guarantee also would be exempt from the registration requirements of the Securities Act even though the guarantee may be issued by a reporting company.

[26] *See Exceptional Producers Holding Company* (August 17, 1989), agents who serve as independent sales representatives for an affiliate of an insurance company are considered ''consultants and advisors'' under Rule 701; *Golfpro, Inc.* (October 3, 1989), golf pros who serve as independent agents for the distribution of golf products through their pro shops considered consultants and advisors; *Herff Jones, Inc.* (November 13, 1990), *Microship Technology, Inc.* (November 4, 1992) and *Optika Imaging Systems, Inc.* (October 1, 1996), independent sales representatives for the distribution of the issuer's products considered consultants and advisors within the meaning of Rule 701; *US Web Corporation* (November 7, 1996), non-employee franchisees considered consultants and advisors within the meaning of Rule 701; and *The Morgan Health Group, Inc.* (December 18, 1995), *Princeton Medical Management Resources, Inc.* (September 12, 1997), *PHM Management, Inc.* (September 12, 1997) and *Talbert Medical Corporation* (September 12, 1997), participating physicians who contract to provide medical services pursuant to various managed care arrangements considered consultants and advisors within the meaning of Rule 701.

[27] *See* Release No. 33–7506.

[28] 15 U.S.C. 77s(a).

[29] 15 U.S.C. 78w(a).

V. Summary of Initial Regulatory Flexibility Analysis

In accordance with 5 U.S.C. 603 we have prepared an initial Regulatory Flexibility Analysis (''IRFA'') regarding the proposed amendments.

The analysis notes that we are proposing the amendments to Rule 701 as a result of:

(i) Concerns expressed to us by practitioners;

(ii) Feedback that the current dollar limitations unduly constrain the ability of many eligible issuers to utilize Rule 701; and

(iii) The specific Congressional mandate expressed in the legislative history of NSMIA. The purpose of the revisions is to remove unnecessary constraints. We have determined that the proposed amendments will not impair investor protection.

As the IRFA describes, we are aware of approximately 1100 Exchange Act reporting companies that currently satisfy the definition of ''small business'' under Rule 157 of the Securities Act.[30] The proposals do not impose any new recordkeeping requirements or require reporting of additional information. Thus, we believe that the proposals will not increase reporting, recordkeeping or compliance burdens, and may reduce those burdens for smaller businesses.

As discussed more fully in the IRFA, several possible significant alternatives to the proposals were considered. These included establishing different compliance or reporting requirements for small entities, exempting them from all or part of the proposed requirements, or requiring them to provide more disclosure, such as more Form 1–A items, more information pursuant to Rule 502 of Regulation D or the full disclosure requirements of Form SB–1 or SB–2. The IRFA also indicates that no current federal rules duplicate, overlap, or conflict with the proposed rule amendments.

We encourage written comments on any aspect of the IRFA. In particular, we seek comment on:

(i) The number of small entities that would be affected by the proposed rule amendments; and

(ii) The determination that the proposed rule amendments would not increase (and in some cases may reduce) reporting, recordkeeping and other compliance requirements for small entities. If you believe the proposals will significantly impact a substantial number of small entities, please describe the nature of the impact and estimate the extent of the impact. For purposes of making determinations required by the Small Business Regulatory Enforcement Fairness Act of 1996 (''SBREFA''),[31] we are also requesting data regarding the potential impact of the proposed amendments on the economy on an annual basis. Your comments will be considered in the preparation of the Final Regulatory Flexibility Analysis if the proposed amendments are adopted. A copy of the Initial Regulatory Flexibility Act Analysis may be obtained from Twanna M. Young, Office of Small Business, Division of Corporation Finance, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

VI. Cost-Benefit Analysis

As an aid in the evaluation of the costs and benefits of these proposals, we request the views and other supporting information of the public. We believe that the proposed rule amendments, if adopted, would result in significant cost savings for issuers without compromising investor protection. We believe that the expanded use of Rule 701 may provide significant savings to small issuers and considerable benefits to compensated persons who in the past may have been deprived of the opportunity to receive securities as an incentive or in payment for their services. We note that during the period from mid-1988 through mid-1993, when persons relying upon the exemption were required to file a report with us concerning reliance on the exemption, that 1,294 filings were made covering approximately $2.28 billion worth of securities.

We request your comment on whether the proposed rule amendments would be a ''major rule'' for purposes of the SBREFA. We have concluded preliminarily that the proposed rule amendments would not result in a major increase in costs or prices for consumers or individual industries, or significant adverse effects on competition, employment, investment, productivity, innovation or small business. We believe that those persons who will rely on the rule will not have significantly increased costs for providing the proposed information since many of these persons either provide to or have such information readily available for their employees and other persons covered by the rule now. We request comments on whether the proposed rule amendments are likely to have an annual effect on the economy of $100 million or more. Your comments should provide empirical data to support your views.

VII. Paperwork Reduction Act

Our staff has consulted with the Office of Management and Budget (''OMB'') and has submitted the proposals for review in accordance with the Paperwork Reduction Act of 1995 (''the Act'').[32] The title to the affected information collection is: ''Rule 701.'' The specific information that must be included is explained in the rule itself, and relates to the issuer and the risk factors that may be associated with investment in securities under the plan or agreement. The information is needed by prospective purchasers to make informed investment decisions.

The proposed amendments, if adopted, would increase the flexibility and utility of Rule 701 for private companies using securities to compensate their employees.

The collection of information in Rule 701 will be required in order for companies to use the rule for sales of their securities to their employees and other persons covered by the rule. The likely respondents to the rule are those companies that have heretofore utilized the rule, but were being constrained by its limits and those private companies who could not utilize the two formulas. While we cannot estimate the number of respondents that may use expanded Rule 701, there were 1,294 Form 701 filings during the period from mid-1988 through mid-1993, when persons relying upon the exemption were required to file a report with us concerning reliance on the exemption. We expect that approximately 300 companies each year will be relying on the exemption. If expanded Rule 701 is adopted, the estimated burden for responding to the collection of information in Rule 701 would not increase for most companies due to the current disclosure requirements in Rule 701, but may increase slightly for other companies who may not be currently providing risk factor information and financial statements to employee purchasers. We estimate that the burden hours per respondent each year will be two. Therefore, we estimate an aggregate of 600 burden hours per year.

The information collection requirements imposed by Rule 701 are mandatory to the extent that a company elects to utilize the Rule 701 exemption. The information will be disclosed to third parties or the public. We may not require a response to the collection of

[30] 17 CFR 230.157.

[31] Pub. L. No. 104–121, 110 Stat. 857 (1996)(codified in scattered sections of 5 U.S.C., 15 U.S.C., and as a note to 5 U.S.C. 601).

[32] 44 U.S.C. 3501 *et seq.*

information if the rule does not display a current valid OMB control number.

In accordance with the Act,[33] we solicit comment on the following: whether the proposed changes in the collection of information is necessary; on the accuracy of our estimate of the burden of the proposed changes to the collection of information; on the quality, utility and clarity of the information to be collected; and whether the burden of collection of information on those who are to respond; including through the use of automated collection techniques or other forms of information technology, may be minimized.

Persons desiring to submit comments on the collection of information requirement should direct them to: Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, D.C. 20503, and should also send a copy of their comments to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549, with reference to File No. S7–5 –98. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication, so a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication.

VIII. Statutory Basis, Text of Proposals and Authority

The amendments to our rules and forms are being proposed pursuant to sections 2, 3(b), 6, 7, 8, 10, 19(a) and 28 of the Securities Act.

List of Subjects in 17 CFR Part 230

Reporting and recordkeeping requirements, Securities.

For the reasons set out in the preamble, title 17, chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

1. The general authority citation for part 230 is revised to read in part as follows:

Authority: 15 U.S.C. 77b, 77f, 77g, 77h, 77j, 77r, 77s, 7sss, 78c, 78d, 78*l*, 78m, 78n, 78o, 78w, 78*ll*(d), 79t, 80a–8, 80a–24, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

* * * * *

2. Section 230.701 is revised to read as follows:

[33] 44 U.S.C. 3506(c)(2)(B).

§ 230.701 Exemption for offers and sales of securities pursuant to certain compensatory benefit plans and contracts relating to compensation.

Preliminary Notes

1. This section relates to transactions exempted from the registration requirements of section 5 of the Act (15 U.S.C. 77e). These transactions are not exempt from the antifraud, civil liability, or other provisions of the federal securities laws. Issuers have an obligation to provide investors with any additional material information as may be necessary to make the information required under this regulation, in light of the circumstances under which it is furnished, not misleading.

2. In addition to complying with this section, the issuer also must comply with any applicable state law relating to the offer and sale of securities.

3. An issuer that attempts to comply with this section, but fails to do so, may claim any other exemption that is available.

4. This section is available only to the issuer of the securities. Affiliates of the issuer may not use this section to offer or sell securities. This section also does not cover resales of securities by any person. This section provides an exemption only for the transactions in which the securities are offered or sold by the issuer, not for the securities themselves.

5. The purpose of this section is to provide an exemption from the registration requirements of the Act for securities issued in compensatory circumstances. This section is not available for plans or schemes to circumvent this purpose, such as to raise capital. This section also is not available to exempt any transaction that is in technical compliance with this section but is part of a plan or scheme to evade the registration provisions of the Act. In any of these cases, registration under the Act is required unless any other exemption is available.

(a) Exemption. Offers and sales made in compliance with all of the conditions of this section are exempt from section 5 of the Act (15 U.S.C. 77e).

(b) Issuers eligible to use the rule—(1) General. This section is available to any issuer that is not subject to the reporting requirements of section 13 or 15(d) of the Securities Exchange Act of 1934 (the ''Exchange Act'') (15 U.S.C. 78m or 78o(d)) and is not an investment company registered or required to be registered under the Investment Company Act of 1940 (15 U.S.C. 80a–1 *et seq.*).

(2) Issuers that become subject to reporting. If an issuer becomes subject to the reporting requirements of section 13 or 15(d) of the Exchange Act (15 U.S.C. 78m or 78o(d)) after it has made offers complying with this section, it may nevertheless rely on this section to sell the securities previously offered to the persons to whom those offers were made.

(3) Guarantees by reporting companies. An issuer subject to the reporting requirements of section 13 or 15(d) of the Exchange Act (15 U.S.C. 78m, 78o(d)) may rely on this section if it is merely guaranteeing the repayment of a subsidiary's securities that are sold under this rule.

(c) Transactions exempted by the rule. This section exempts offers and sales of securities (including plan interests and guarantees pursuant to § 230.701(d)(1)(ii)) under a written compensatory benefit plan (or written compensation contract) established by the issuer, its parents, its majority-owned subsidiaries or majority-owned subsidiaries of the issuer's parent, for the participation of their employees, former employees, directors, general partners, trustees (where the issuer is a business trust), or consultants and advisors, and their immediate family who acquire such securities from such persons through gifts or domestic relations orders. In the case of a former employee, this section exempts offers and sales only if the former employee was employed by the issuer at the time the securities were offered to the employee.

(1) Special requirements for consultants and advisors. This section is only available if bona fide services are provided by the consultants or advisors that are natural persons and the services are not provided in connection with the offer and sale of securities in a capital-raising transaction.

(2) Definition of ''Compensatory benefit plan''. For purposes of this section, a *compensatory benefit plan* is any purchase, savings, option, bonus, stock appreciation, profit sharing, thrift, incentive, deferred compensation, pension or similar plan.

(d) Amounts that may be sold—(1) Offers. Any amount may be offered in reliance on this section.

(2) Sales. The aggregate sales price or amount of securities sold in reliance on this section in any consecutive 12-month period, shall not exceed the *greatest* of the following:

(i) $1,000,000;

(ii) 15% of the total assets of the issuer (or of the issuer's parent if the issuer is a wholly-owned subsidiary and the securities represent obligations that the parent fully and unconditionally

guarantees), measured at the issuer's most recent balance sheet date; or

(iii) 15% of the outstanding amount of the class of securities being offered and sold in reliance on this section, measured at the issuer's most recent balance sheet date.

(3) Rules for calculating prices and amounts—(i) Aggregate sales price. The term aggregate sales price means the sum of all cash, property, notes, cancellation of debt or other consideration received or to be received by the issuer for the sale of the securities. Non-cash consideration must be valued by reference to *bona fide* sales of that consideration made within a reasonable time or, in the absence of such sales, on the fair value as determined by an accepted standard. The value of services exchanged for securities issued to employees, as well as to consultants and advisors, should be included in the aggregate sales price.

(ii) Derivative securities. In calculating outstanding securities for purposes of paragraph (d)(2)(iii) of this section, treat the securities underlying all currently exercisable or convertible options, warrants, rights or other securities, other than those issued under this section, as outstanding. In calculating the amount of securities sold for purposes of paragraph (d)(1) of this section, count the amount of securities that would be acquired upon exercise or conversion in connection with sales of options, warrants, rights or other exercisable or convertible securities.

(iii) Other exemptions. Amounts of securities sold in reliance on this section do not affect amounts that may be sold in reliance on other exemptions, and amounts of securities sold in reliance on other exemptions do not affect amounts that may be sold in reliance on this section.

(e) Disclosure that must be provided—The issuer must deliver the following disclosure to investors a reasonable period of time prior to the date of sale:

(1) A copy of the compensatory benefit plan or the contract, as applicable;

(2) If the plan is subject to the Employee Retirement

Income Security Act of 1974 (''ERISA'') (29 U.S.C. 1104–1107), a copy of the summary plan description required by ERISA;

(3) If the plan is not subject to ERISA, a summary of the material terms of the plan;

(4) Information about the risks associated with investment in the securities sold pursuant to the compensatory benefit plan or compensation contract; and

(5) Financial statements required to be furnished by Part F/S of Form 1–A (Regulation A Offering Statement) (§ 239.90 of this chapter). Such financial statements must be as of a date no more than 180 days prior to the sale of securities in reliance on this section. If the issuer is relying on § 230.701(d)(2)(ii) to use its parent's total assets to determine the amount of securities that may be sold, the parent's financial statements must be delivered. If the parent is subject to the reporting requirements of section 13 or 15(d) of the Exchange Act (15 U.S.C. 78m or 78o(d)), the financial statements of the parent required by Rule 10–01 of Regulation S–X (§ 210.10–01 of this chapter) and Item 310 of Regulation S–B (§ 228.310 of this chapter), as applicable, must be delivered.

(6) If the sale involves a stock option or other exercisable or convertible security, the issuer must deliver disclosure a reasonable period of time prior to the date of exercise or conversion. For deferred compensation or similar plans, the issuer must deliver disclosure to investors a reasonable period of time prior to the date the irrevocable election to defer is made.

(f) No integration with other offerings. Offers and sales exempt under this section are deemed to be a part of a single, discrete offering and are not subject to integration with any other offers or sales, whether registered under the Act or otherwise exempt from the registration requirements of the Act.

(g) Resale limitations—(1) Securities issued pursuant to this section are deemed to be ''restricted securities'' as defined in § 230.144.

(2) Resales of securities issued pursuant to this section must be in compliance with the registration requirements of the Act or an exemption therefrom.

(3) Ninety days after the issuer becomes subject to the reporting requirements of section 13 or 15(d) of the Exchange Act (15 U.S.C. 78m or 78o(d)), securities issued pursuant to this section may be resold by persons who are not affiliates (as defined in § 230.144) in reliance on § 230.144 without compliance with paragraphs (c), (d), (e) and (h) of § 230.144, and by affiliates without compliance with paragraph (d) of § 230.144.

By the Commission.

Dated: February 27, 1998.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 98–5728 Filed 3–4–98; 8:45 am]

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DEPARTMENT OF HEALTH AND HUMAN SERVICES

Food and Drug Administration

21 CFR Parts 809 and 864

[Docket No. 97N–0135]

Hematology and Pathology Devices; Reclassification; Restricted Devices; OTC Test Sample Collection Systems for Drugs of Abuse Testing

AGENCY: Food and Drug Administration, HHS.

ACTION: Proposed rule.

SUMMARY: The Food and Drug Administration (FDA) is proposing to reclassify over-the-counter (OTC) test sample collection systems for drugs of abuse testing from class III (premarket approval) into class I (general controls), and to exempt them from the premarket notification (510(k)) and current good manufacturing practice (CGMP) requirements. FDA is also proposing to designate OTC test sample collection systems for drugs of abuse testing as restricted devices under the Federal Food, Drug, and Cosmetic Act (the act), and to establish restrictions intended to assure consumers that: The underlying laboratory test(s) are accurate and reliable; the laboratory performing the test(s) has adequate expertise and competency; and the product has adequate labeling and methods of communicating test results to consumers. Finally, FDA is proposing a conforming amendment to the existing classification regulation for specimen transport and storage containers, to clarify that it does not apply to specimen transport and storage containers that are part of an OTC test sample collection system for the purpose of testing for the presence of drugs of abuse or their metabolites in a laboratory.

DATES: Written comments on the proposed rule by July 6, 1998. FDA proposes that any final regulation based on this proposal become effective 1 year after its date of publication in the **Federal Register**.

Written comments on the information collection requirements should be submitted by April 6, 1998.

ADDRESSES: Submit written comments on the proposed rule to the Dockets Management Branch (HFA–305), Food and Drug Administration, 12420 Parklawn Dr., rm. 1–23, Rockville, MD 20857.

Submit written comments on the information collection requirements to the Office of Information and Regulatory