

**SECURITIES AND EXCHANGE  
COMMISSION****17 CFR Parts 230 and 239**

[Release No. 33-8878; File No. S7-10-07]

RIN 3235-AJ89

**Revisions to the Eligibility  
Requirements for Primary Securities  
Offerings on Forms S-3 and F-3****AGENCY:** Securities and Exchange  
Commission.**ACTION:** Final rule.

**SUMMARY:** We are adopting amendments to the eligibility requirements of Form S-3 and Form F-3 to allow certain domestic and foreign private issuers to conduct primary securities offerings on these forms without regard to the size of their public float or the rating of debt they are offering, so long as they satisfy the other eligibility conditions of the respective form, have a class of common equity securities listed and registered on a national securities exchange, and the issuers do not sell more than the equivalent of one-third of their public float in primary offerings over any period of 12 calendar months. The amendments are intended to allow more companies to benefit from the greater flexibility and efficiency in accessing the public securities markets afforded by Form S-3 and Form F-3 without compromising investor protection. The expanded form eligibility does not extend to shell companies, however, which are prohibited from using the new provisions until 12 calendar months after they cease being shell companies. In addition, we are adopting an amendment to the rules and regulations promulgated under the Securities Act to clarify that violations of the one-third restriction will also violate the requirements as to proper registration form, even though the registration statement has been declared effective previously.

**EFFECTIVE DATE:** January 28, 2008.

**FOR FURTHER INFORMATION CONTACT:** Raymond A. Be, at (202) 551-3430, or the Office of Chief Counsel, at (202) 551-3500, in the Division of Corporation Finance, U.S. Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-3010.

**SUPPLEMENTARY INFORMATION:** We are amending Form S-3,<sup>1</sup> Form F-3<sup>2</sup> and

Rule 401(g)<sup>3</sup> under the Securities Act of 1933.<sup>4</sup>

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**I. Discussion****A. Background****1. Proposing Release and Public Comment Letters**

On May 23, 2007, we proposed revisions to the eligibility requirements of Form S-3 and Form F-3 to allow domestic and foreign private issuers, respectively, to conduct primary securities offerings on these forms without regard to the size of their public float or the rating of debt they are offering, so long as they satisfy the other eligibility conditions of the applicable form and do not sell securities valued in excess of 20% of their public float in primary offerings pursuant to the new instructions on these forms over any period of 12 calendar months.<sup>5</sup>

In response to our request for comment on the Proposing Release, we received comment letters from a variety

of groups and constituencies, most of whom expressed their general support for the proposed form amendments and the objectives that we articulated in the Proposing Release. Notwithstanding their general support, however, several commenters thought that some modifications to the proposal were advisable, either to improve the usefulness of the form amendments to smaller public companies seeking capital,<sup>6</sup> or to ensure that the rule changes are consistent with investor protection.<sup>7</sup> After considering each of the comments, we are adopting amendments to Form S-3 and Form F-3 substantially in the form proposed, but with certain modifications as discussed more fully in this release.

These amendments are intended to allow a larger number of public companies to benefit from the greater flexibility and efficiency in accessing the public securities markets afforded by Form S-3 and Form F-3 in a manner that is consistent with investor protection. Accordingly, we are placing certain restrictions on the class of issuers who will be eligible under the new rules and are adopting a ceiling on the amount of securities that eligible issuers may offer pursuant to these rules. In creating new opportunities to facilitate capital formation consistent with the protection of investors, we believe that a careful and modest expansion of Form S-3 and Form F-3 eligibility is warranted at this time. However, as we indicated in the Proposing Release, we may revisit the appropriateness of the form restrictions at a later time if our experience with this revised requirement suggests issuer eligibility for primary offerings on Form S-3 and Form F-3 should be further revised.<sup>8</sup>

**2. Form S-3**

Form S-3 is the "short form" used by eligible domestic companies to register securities offerings under the Securities Act of 1933. The form also allows these companies to rely on their reports filed under the Securities Exchange Act of

<sup>6</sup> See, for example, letters from the American Bar Association, Committees on Federal Regulation of Securities and State Regulation of Securities ("ABA"); Brinson Patrick Securities Corporation ("Brinson Patrick"); Feldman Weinstein and Smith LLP ("Feldman Weinstein"); Malizia Spidi & Fisch ("Malizia Spidi"); Morrison & Foerster LLP ("Morrison & Foerster"); Office of Advocacy, Small Business Administration ("SBA"); Roth Capital Partners, LLP ("Roth Capital"); Marshal Shichtman ("M. Shichtman"); and Williams Securities Law ("Williams Securities"). All comment letters are publicly available at <http://www.sec.gov/comments/s7-10-07/s71007.shtml>.

<sup>7</sup> See letter from the Council of Institutional Investors ("CII").

<sup>8</sup> Proposing Release, at 35124.

<sup>3</sup> 17 CFR 230.401(g).

<sup>4</sup> 15 U.S.C. 77a et seq.

<sup>5</sup> *Revisions to the Eligibility Requirements for Primary Securities Offerings on Forms S-3 and F-3*, Release No. 33-8812 (June 20, 2007) [72 FR 35118] (the "Proposing Release").

<sup>1</sup> 17 CFR 239.13.

<sup>2</sup> 17 CFR 239.33.

1934<sup>9</sup> to satisfy the form's disclosure requirements. Prior to today's amendments, companies have been able to register *primary* offerings (that is, securities offered by or on behalf of the registrant for its own account) on Form S-3 only if their non-affiliate equity market capitalization, or "public float," was \$75 million or more.<sup>10</sup> In contrast, transactions involving primary offerings of non-convertible investment grade securities, certain rights offerings, dividend reinvestment plans and conversions, and offerings by selling shareholders of securities registered on a national securities exchange do not require the company to have a minimum public float.<sup>11</sup>

Recently, the issue of Form S-3 eligibility for primary offerings was addressed by the Commission's Advisory Committee on Smaller Public Companies (the "Advisory Committee"), which the Commission chartered in 2005 to assess the current regulatory system for smaller companies under U.S. securities laws.<sup>12</sup> In its April 23, 2006 Final Report to the Commission, the Advisory Committee recommended that we allow all reporting companies with securities listed on a national securities exchange or Nasdaq,<sup>13</sup> or quoted on the Over-the-Counter Bulletin Board electronic quotation service, to be eligible to use Form S-3 if they have been reporting under the Exchange Act for at least one year and are current in their reporting at the time of filing.<sup>14</sup>

### 3. Reasons for New Form S-3 Amendments

The ability to conduct primary offerings on Form S-3 confers

significant advantages on eligible companies.<sup>15</sup> Form S-3 permits the incorporation of required information by reference to a company's disclosure in its Exchange Act filings, including Exchange Act reports that were previously filed and those that will be filed in the future.<sup>16</sup>

Form S-3 eligibility for primary offerings also enables companies to conduct primary offerings "off the shelf" under Rule 415 of the Securities Act.<sup>17</sup> Rule 415 provides considerable flexibility in accessing the public securities markets from time to time in response to changes in the markets and other factors. The shelf eligibility resulting from Form S-3 eligibility and the ability to forward incorporate information on Form S-3, therefore, allow companies to avoid additional delays and interruptions in the offering process and can reduce or even eliminate the costs associated with preparing and filing post-effective amendments to the registration statement.

By having more control over the timing of their offerings, these companies can take advantage of desirable market conditions, thus allowing them to raise capital on more favorable terms (such as pricing) or to obtain lower interest rates on debt. As a result, the ability to take securities off the shelf as needed gives issuers a significant financing alternative to other widely available methods, such as private placements with shares usually priced at discounted values based in part on their relative illiquidity.<sup>18</sup> Consequently, we believe that extending Form S-3 short-form registration to additional issuers should enhance their

ability to access the public securities markets. Likewise, a significant proportion of commenters to the Proposing Release welcomed an expansion of Form S-3 eligibility, agreeing that such a measure would greatly enhance smaller public companies' access to capital in the securities markets, with far less burden and cost.<sup>19</sup>

Given the great advances in the electronic dissemination and accessibility of company disclosure transmitted over the Internet in the last several years,<sup>20</sup> we believe that moderately expanding the class of transactions that are permitted on Form S-3 for primary securities offerings is warranted once again. In contrast to 1992, when the Commission last adjusted the issuer eligibility requirements for Form S-3,<sup>21</sup> most public filings under the Securities Act and the Exchange Act, and all Forms S-3, are now filed on the Commission's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR"). The pervasiveness of the Internet in daily life and the advent of EDGAR as a central repository of company filings have combined to allow widespread, direct, and contemporaneous accessibility to company disclosure at little or no cost to those interested in obtaining the information. For this reason, we think it is appropriate to once again expand the class of companies who may register primary offerings on Form S-3 in a limited manner.

### 4. Limited Expansion of Form Eligibility

We are not prepared at this time to abandon our longstanding prerequisite contained in the instructions to Form S-3 and allow unlimited use of this form for primary offerings by companies who do not have at least \$75 million in

<sup>9</sup> 15 U.S.C. 78a *et seq.*

<sup>10</sup> General Instruction I.B.1. of Form S-3. The history and use of Form S-3 are discussed in greater detail in the Proposing Release.

<sup>11</sup> See General Instructions I.B.2. through I.B.4. of Form S-3.

<sup>12</sup> More information about the Advisory Committee is available at <http://www.sec.gov/info/smallbus/acspc.shtml>.

<sup>13</sup> There is no longer a distinction between Nasdaq and national securities exchanges. On January 13, 2006, the Commission approved Nasdaq's application to become a national securities exchange. The Nasdaq Stock Market commenced operations on August 1, 2006.

<sup>14</sup> Recommendation IV.P.3. of the Final Report of the Advisory Committee on Smaller Public Companies (Apr. 23, 2006) (the "Final Report"), at 68-72. The Final Report is available at <http://www.sec.gov/info/smallbus/acspc/acspc-finalreport.pdf>. In addition to elimination of the public float requirement, Recommendation IV.P.3. also called for (1) elimination of General Instruction I.A.3.(b) to Form S-3 requiring that the issuer has timely filed all required reports in the last year and (2) extending Form S-3 eligibility for secondary transactions to issuers quoted on the Over-the-Counter Bulletin Board. The Proposing Release also included additional discussion of the Advisory Committee and its recommendations.

<sup>15</sup> See generally, *Shelf Registration*, Release No. 33-6499 (Nov. 17, 1983) [48 FR 5289] (discussing the benefits of shelf registration).

<sup>16</sup> Item 12 of Form S-3: "Incorporation of Certain Information by Reference."

<sup>17</sup> Rule 415 [17 CFR 230.415] provides that:

(a) Securities may be registered for an offering to be made on a continuous or delayed basis in the future, *Provided*, That:

(1) the registration statement pertains only to:

\* \* \*

(x) Securities registered (or qualified to be registered) on Form S-3 or Form F-3 which are to be offered and sold on an immediate, continuous or delayed basis by or on behalf of the registrant, a majority owned subsidiary of the registrant or a person of which the registrant is a majority-owned subsidiary.

<sup>18</sup> See, for example, Susan Chaplinsky and David Haushalter, *Financing Under Extreme Uncertainty: Contract Terms and Returns to Private Investments in Public Equity* (May 2006), available at: [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=907676](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=907676) (discussing the typical contractual terms of PIPEs (Private Investments in Public Equities) financings, where the average purchase discount is between 18.5% to 19.7%, depending on the types of contractual rights embedded in the securities).

<sup>19</sup> See, for example, letters from Feldman Weinstein; Malizia Spidi; and M. Shichtman.

<sup>20</sup> See, for example, *Internet Availability of Proxy Materials*, Release No. 34-52926 (Dec. 8, 2005) [70 FR 74597] and the Final Report of the Advisory Committee, at 69.

The Commission has recently taken several steps acknowledging the widespread accessibility over the Internet of documents filed with the Commission. In its recent release concerning Internet delivery of proxy materials, the Commission notes that recent data indicates that up to 75% of Americans have access to the Internet in their homes, and that this percentage is increasing steadily among all age groups. As a result we believe that investor protection would not be materially diminished if all reporting companies on a national securities exchange, NASDAQ or the Over-the-Counter Bulletin Board were permitted to utilize Form S-3 and the associated benefits of incorporation by reference.

<sup>21</sup> *Simplification of Registration Procedures for Primary Securities Offerings*, Release No. 33-6964 (Oct. 22, 1992) [57 FR 48970].

public float. Although the Advisory Committee recommended the qualified elimination of this requirement<sup>22</sup> and some commenters supported removing the concept of float altogether as a criterion of eligibility,<sup>23</sup> we believe that retaining some capitalization restrictions on Form S-3 eligibility is still advisable. We are persuaded that the technological advances that have revolutionized communications between companies and the market should allow us to ease the Form S-3 eligibility standards without undermining investor protection or the integrity of the markets. However, as explained more fully below, we believe this warrants only the limited expansion of certain offerings on Form S-3, not the wholesale elimination of public float as an important criterion of form eligibility. The Commission's system of integrated disclosure has, since its inception, been premised on the idea that a company's disclosure in its registration statement can be streamlined to the extent that the market has already taken that information into account.<sup>24</sup> Public float has for many years been used as an approximate measure of a stock's market following and, consequently, the degree of efficiency with which the market absorbs information and reflects it in the price of a security.<sup>25</sup> While current

technology provides investors with access to information about publicly reporting companies at an unprecedented level of ease and speed, it does not guarantee that the market has fully absorbed and synthesized all of the available information of a given company. Technology can facilitate and enhance market following, but it does not ensure it. Therefore, we are retaining public float as a factor in determining the extent of short-form eligibility. While the purpose of these amendments is to give smaller companies added flexibility to quickly respond to favorable market conditions by conducting some primary shelf offerings on Form S-3, this objective must be balanced against the imperatives of investor protection.

Concerns have been raised in the past when the Commission considered easing the restrictions of shelf registration eligibility to allow smaller public companies to use a modified form of shelf registration,<sup>26</sup> and similar concerns were voiced again during the comment period.<sup>27</sup> It has been observed that the securities of smaller public companies are comparatively more vulnerable to price manipulation than the securities of larger public companies,<sup>28</sup> and may also be more prone to financial reporting error and abuses.<sup>29</sup> As we stated in the Proposing

Release, although we believe that the public securities markets have benefited from advances in both technology and corporate disclosure requirements, we are nevertheless mindful that companies with a smaller market capitalization as a group have a comparatively smaller market following than larger, well-seasoned issuers and are more thinly traded. In such markets, the potential for manipulative practices is more acute.<sup>30</sup> As such, we are sensitive to the market effects of loosening the standards for shelf eligibility without limitation.

We also note that the disclosure obligations and liability imposed by the federal securities laws on smaller public companies are comparable, but not identical, to the largest reporting companies.<sup>31</sup> We are comfortable that

reporting errors at smaller public companies "tend to be more significant" than those of larger companies; and (2) smaller public companies "are more likely to sit on errors that decrease earnings than big companies." Thus, the Commission should ensure that the final rule avoids understating the significant risks that smaller public companies present to investors [emphasis in original].

<sup>30</sup>The Commission's staff has stated previously that, with respect to short sales in reliance on the safe harbor of Rule 144 where the borrower closes out using the restricted securities, all the conditions of Rule 144 must be met at the time of the short sale. See Questions 80 through 82 of *Resales of Restricted and Other Securities*, Release No. 33-6099 (Aug. 2, 1979) [44 FR 46752, 46765]. In the Commission's view, the term "sale" under the Securities Act includes contract of sale. See *Securities Offering Reform*, Release No. 33-8591 (Jul. 19, 2005) [70 FR 44722, 44765] and *Short Selling in Connection With a Public Offering*, Release No. 34-56206 (Aug. 6, 2007) [72 FR 45094]. The Commission has previously indicated that, in a short sale, the sale of securities occurs at the time the short position is established, rather than when shares are delivered to close out that short position, for purposes of Section 5 of the Securities Act. See, for example, Questions 3 and 5 of *Commission Guidance on the Application of Certain Provisions of the Securities Act of 1933, the Securities Exchange Act of 1934, and Rules Thereunder to Trading in Security Futures Products*, Release No. 33-8107 (June 21, 2002) [67 FR 43234] and Release No. 34-56206 n. 46 (Aug. 6, 2007) [72 FR 45094, 45096].

<sup>31</sup>Beginning with its introduction in 1992, Regulation S-B of the Securities Act provided for a scaled set of disclosure requirements for small business issuers. *Small Business Initiatives*, Release No. 33-6949 (July 30, 1992) [57 FR 36442]. Recent amendments to the disclosure regime for smaller companies maintain these scaled disclosure requirements, but integrate them into Regulation S-K. *Smaller Reporting Company Regulatory Relief and Simplification*, Release No. 33-8876 (Dec. 19, 2007).

In addition, we acknowledge that the companies implicated in this rulemaking are not yet fully subject to Section 404 of Sarbanes-Oxley. See *Internal Control Over Financial Reporting in Exchange Act Periodic Reports of Non-Accelerated Filers and Newly Public Companies*, Release No. 33-8760 (Dec. 15, 2006) [71 FR 76580]. We have taken steps to implement a plan to improve the efficiency and effectiveness of Section 404 implementation, including its scalability to smaller companies. See *Commission Guidance Regarding Management's Report on Internal Control Over*

<sup>22</sup> The Advisory Committee's recommendation to expand Form S-3 eligibility encompassed only companies whose securities are listed on a national securities exchange or Nasdaq (which, at the time, was not yet a national securities exchange), or quoted on the Over-the Counter Bulletin Board. Refer to Recommendation IV.P.3. of the Final Report.

<sup>23</sup> See letters from the ABA; Morrison & Foerster; and Roth Capital.

<sup>24</sup> See Release No. 33-6499, at 5:

Forms S-3 and F-3 recognize the applicability of the efficient market theory to those companies which provide a steady stream of high quality corporate information to the marketplace and whose corporate information is broadly disseminated. Information about these companies is constantly digested and synthesized by financial analysts, who act as essential conduits in the continuous flow of information to investors, and is broadly disseminated on a timely basis by the financial press and other participants in the marketplace. Accordingly, at the time S-3/F-3 registrants determine to make an offering of securities, a large amount of information already has been disseminated to and digested by the marketplace.

See also Harold S. Bloomenthal and Samuel Wolff, *Securities and Federal Corporate Law*, § 9:30, available through Westlaw at 3B Sec. & Fed. Corp. Law § 9:30 (2d. ed.) ("Form S-3 epitomizes the efficient market concept."). See also Randall S. Thomas and James F. Cotter, *Measuring Securities Market Efficiency in the Regulatory Setting*, 63 Law & Contemp. Probs. 105 (2000) at 106.

<sup>25</sup> See *Reproposal of Comprehensive Revision to System for Registration of Securities Offerings*, Release No. 33-6331 (Aug. 6, 1981) [46 FR 41902], at 9: "The Commission views as significant the strong relationship between float and information

dissemination to the market and following by investment institutions." See also Thomas and Cotter, *Measuring Securities Market Efficiency in the Regulatory Setting*, at 108 (stating that the numerical thresholds of Form S-3 were intended to be a rough proxy for which companies were widely followed by the investment community).

<sup>26</sup> See, for example, *Report of the Task Force on Disclosure Simplification* (Mar. 5, 1996), available at <http://www.sec.gov/news/studies/smpl.htm>. See also *Delayed Pricing for Certain Registrants*, Release No. 33-7393 (Feb. 20, 1997) [62 FR 9276].

<sup>27</sup> See letter from the CII.

<sup>28</sup> See, for example, Rajesh Aggarwal and Guojun Wu, *Stock Market Manipulations*, 79 Journal of Business, No. 4 (2006). The authors' data indicate that manipulative practices predominantly occur in the Over-the-Counter Bulletin Board, Pink Sheets and other regional or unidentified markets characterized by very low average trading volume and market capitalization. The authors conclude that stock manipulation is more likely to occur "in relatively inefficient markets \* \* \* that are small and illiquid."

<sup>29</sup> In its letter commenting on the Proposing Release, the CII "strongly opposed any weakening of the proposed limitations on eligibility in the final rule," stating:

We share the Commission's concerns that the Proposed Rule presents "risks to investor protection by expanding the base of companies eligible for primary offerings" on Forms S-3 and F-3 \* \* \* In addition [to the risks discussed by the Commission in the Proposing Release], we believe that the final rule should explicitly acknowledge that smaller public companies have long been especially prone to financial reporting fraud. Consistent with the historical evidence, a recent analysis of the reporting by public companies in response to SEC Staff Accounting Bulletin 108 found that (1)

the scaled disclosure standards for smaller public companies are sufficiently comparable to those governing larger issuers such that the limited expansion of Form S-3 primary offering eligibility, as we are adopting it, will not adversely impact investors. However, the level of disclosure required of smaller public companies under the federal securities laws is yet another factor that we believe weighs against expanding Form S-3 eligibility further than we have in this release.<sup>32</sup>

In revising the shelf eligibility requirements, therefore, we must consider the unique set of investment risks posed by smaller public companies in the context of shelf registration, which provides speed and flexibility to issuers, but at the same time may limit Commission and underwriter involvement in the registration process. Extending the benefits of shelf registration to an expanded group of transactions will limit the staff's direct prior involvement in takedowns of securities off the shelf. Although the Commission's staff may review registration statements before they are declared effective, individual takedowns are not conditioned on further Commission action or subject to prior selective staff review.<sup>33</sup> In

*Financial Reporting Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934*, Release No. 34-55929 (June 20, 2007) [72 FR 35323]. It is true, however, that, unlike "large accelerated filers" and "accelerated filers," companies that are "non-accelerated filers" (companies with less than \$75 million in float) will not need to comply with the auditor's attestation report requirements of Section 404 until they file their annual report for the fiscal year ending on or after December 15, 2008. For large accelerated filers and accelerated filers, the auditor's attestation report is required for all annual reports for fiscal years ending on or after November 15, 2004. In light of this fact, one commenter recommended that Form S-3 eligibility be contingent on full implementation of both the management and auditor attestation report requirements of Section 404. See letter from the CII. Because adding this condition would effectively delay the benefits of these Form S-3 amendments to smaller public companies for at least one year, and because the decision has been made to allow smaller public companies to phase in full compliance with Section 404, we have decided not to delay the effective date of this rulemaking. We may revisit the limitation on our expansion of Form S-3 after full compliance with Section 404 is complete.

<sup>32</sup> This is especially true given that, under recent amendments, the scaled detailed disclosure regime for smaller companies will now extend to issuers who have a public float between \$25 and \$75 million. Release No. 33-8876. Prior to such amendments, only companies with less than \$25 million in public float were covered by the disclosure requirements of Regulation S-B.

<sup>33</sup> We note some commenters suggested that our concerns about expanding the base of companies eligible to use Form S-3 for primary offerings "off the shelf" could be alleviated by requiring more detailed disclosure from these companies. See letters from Feldman Weinstein and Morrison & Foerster. However, requiring additional disclosure

in addition, the short time horizon of shelf offerings may also reduce the time that participating underwriters have to apply their independent scrutiny and judgment to an issuer's prospectus disclosure. Historically, concerns such as these have been at the center of the debate when the Commission has previously considered expanding shelf registration eligibility.<sup>34</sup>

Accordingly, since the Commission first introduced the system of integrated disclosure more than twenty-five years ago, the ability to use Form S-3 to conduct primary offerings "off the shelf" has been carefully tempered by restricting the class of companies eligible for this benefit. Consistent with this well-established approach, we are amending the Form S-3 eligibility requirements to enable more companies to use Form S-3 for primary offerings.<sup>35</sup>

would not address the fact that the staff does not have the ability to review, in advance, individual takedowns off an effective shelf registration statement. Prospectus supplements reflecting such takedowns are filed after the fact. Similarly, the fact that the Form S-3 filed by reporting companies with smaller public floats would not become automatically effective and would therefore remain subject to pre-effective review and comment by the Commission's staff does not satisfactorily address the lack of the staff's prior involvement in shelf takedowns. See letter from the ABA.

<sup>34</sup> Among other things, the Commission's 1996 Task Force on Disclosure Simplification made several recommendations to amend the shelf registration procedure "so as to provide increased flexibility to a wider array of companies with respect to their capital-raising activities." These recommendations included a "modified form of shelf registration" that would have allowed smaller companies to price their securities on a delayed basis for up to one year in order to time securities offerings more effectively with opportunities in the marketplace. The Task Force stated:

While this recommendation will afford small companies time and cost savings, the Task Force appreciates concerns raised about possible adverse effects shelf registration may have on the adequacy and accuracy of disclosures provided to investors, on Commission oversight of the disclosures and on the role of underwriters in the registration process. These concerns are similar to those raised when the shelf registration rule was first being considered on a temporary basis and was made available to any offering including an initial public offering.

*Report of the Task Force on Disclosure Simplification*, at 33. Following on the Task Force's recommendations, in 1997 the Commission proposed to permit certain smaller companies to price registered securities offerings on a delayed basis for up to one year after effectiveness. Release No. 33-7393. In that release, the Commission noted:

Concerns have been raised that the expedited access to the markets that would be provided by these proposals could make it difficult for gatekeepers, particularly underwriters, to perform adequate due diligence for the smaller companies that would be eligible to use expanded Rule 430A.

<sup>35</sup> As part of Recommendation IV.P.3 of the Final Report, the Advisory Committee also recommended that the Commission extend S-3 eligibility for secondary transactions to issuers with securities quoted on the Over-the-Counter Bulletin Board. General Instruction I.B.3. to Form S-3 limits the use of the form for secondary offerings to securities "listed and registered on a national securities

but only to the extent that they are consistent with investor protection.

#### B. Amendments to Form S-3

We are adopting new General Instruction I.B.6. to Form S-3 to allow companies with less than \$75 million in public float to register primary offerings of their securities on Form S-3,<sup>36</sup> provided they:

- Meet the other registrant eligibility conditions for the use of Form S-3;<sup>37</sup>

exchange or \* \* \* quoted on the automated quotation system of a national securities association," a restriction that excludes the securities of Over-the-Counter Bulletin Board and Pink Sheets issuers. In addition, some commenters to the Proposing Release echoed the recommendation of the Advisory Committee and supported extending the use of Form S-3 for secondary offerings to additional issuers who are ineligible under current rules. See letters from the ABA; Feldman Weinstein; SBA; and Williams Securities. After considering the recommendation of the Advisory Committee and commenters, we are not at this time amending the Form S-3 eligibility rules for secondary offerings. As we made clear in the Proposing Release, this rulemaking pertains only to the limited issue of Form S-3 eligibility for primary securities offerings and is not intended to encompass or otherwise impact existing requirements for secondary offerings on Form S-3. Moreover, any amendment of the Form S-3 requirements for secondary offerings would have to be carefully weighed against the costs of further exposing the markets to the potential for abusive primary offerings disguised as secondary offerings. Therefore, at this time we are not revising secondary offering eligibility under General Instruction I.B.3.

<sup>36</sup> Form S-3 eligibility under new General Instruction I.B.6. (and Form F-3 eligibility under new General Instruction I.B.5.) applies only to an issuer's ability to conduct a limited primary offering on Form S-3 (or Form F-3, as applicable). That is, an issuer's eligibility to use Form S-3 or Form F-3 under these new form instructions does not mean that the issuer meets the requirements of Form S-3 or Form F-3 for purposes of any other rule or regulation of the Commission (apart from Rule 415(a)(1)(x), which pertains to shelf registration). Instruction 6 to new General Instruction I.B.6. of Form S-3 and Instruction 6 to new General Instruction I.B.5. of Form F-3.

Rule 415(a)(1)(x) permits shelf offerings of securities "registered (or qualified to be registered)" on Form S-3 or Form F-3 (emphasis added). We note that a closed-end investment company, including a business development company, ("closed-end fund") that meets the eligibility standards enumerated in Form S-3, as revised by new General Instruction I.B.6., may register its securities in reliance on Rule 415(a)(1)(x) notwithstanding the fact that closed-end funds register their securities on Form N-2 rather than Form S-3.

<sup>37</sup> See General Instruction I.A. of Form S-3. Among other things, General Instruction I.A. requires that the registrant:

- Has a class of securities registered pursuant to Sections 12(b) or 12(g) of the Exchange Act or is required to file reports pursuant to Section 15(d) of the Exchange Act; and
- Has been subject to the requirements of Sections 12 or 15(d) of the Exchange Act and has filed in a timely manner all the material required to be filed pursuant to Sections 13, 14 or 15(d) for a period of at least twelve calendar months immediately preceding the filing of the Form S-3 registration statement.

- Have a class of common equity securities that is listed and registered on a national securities exchange;<sup>38</sup>
- Do not sell more than the equivalent of one-third of their public float in primary offerings under General Instruction I.B.6. of Form S-3 over the previous period of 12 calendar months;<sup>39</sup> and
- Are not shell companies<sup>40</sup> and have not been shell companies for at least 12 calendar months before filing the registration statement.

### 1. One-Third Cap and Listed Securities Only

As discussed above, we are sensitive to the risks associated with making shelf registration available to more issuers. At the same time, we are also sensitive to the possibility that constraining the rule too much may limit its utility to the companies that qualify for its use. Therefore, we have decided to increase the limitation on the amount of securities that can be offered by companies under the new rules from 20% of public float to one-third of public float, while at the same time conditioning a company's eligibility

<sup>38</sup> A "national securities exchange" is a securities exchange that has registered with the Commission under Section 6 of the Exchange Act [15 U.S.C. 78f]. There are currently ten securities exchanges registered under Section 6(a) of the Exchange Act as national securities exchanges. These are the New York Stock Exchange, American Stock Exchange and Nasdaq, as well as the Boston Stock Exchange, Chicago Board Options Exchange, Chicago Stock Exchange, International Securities Exchange, National Stock Exchange (formerly the Cincinnati Stock Exchange), NYSE Arca (formerly the Pacific Exchange) and the Philadelphia Stock Exchange. In addition, an exchange that lists or trades security futures products (as defined in Section 3(a)(56) of the Exchange Act [15 U.S.C. 78c(56)]) may register as a national securities exchange under Section 6(g) of the Exchange Act solely for the purpose of trading security futures products. For purposes of new General Instruction I.B.6., however, only exchanges registered under Section 6(a) of the Exchange Act will be deemed to be "national securities exchanges." Instruction 8 to new General Instruction I.B.6.

<sup>39</sup> The meaning of the phrase "period of 12 calendar months" is intended to be consistent with the way in which the phrase "12 calendar months" is used for purposes of the registrant eligibility requirements in Form S-3. A "calendar month" is a month beginning on the first day of the month and ending on the last day of that month. For example, for purposes of Form S-3 registrant eligibility, if a registrant were not timely on a Form 10-Q due on September 15, 2006, but was timely thereafter, it would first be eligible to use Form S-3 on October 1, 2007. Similarly, for purposes of new General Instruction I.B.6. of Form S-3, if a registrant relies on this Instruction to conduct a shelf takedown equivalent to one-third of its public float on September 15, 2007, it will next be eligible to do another takedown (assuming no change in its float) on October 1, 2008.

<sup>40</sup> The term "shell company" is defined in Rule 405 of the Securities Act [17 CFR 230.405]. See also *Use of Form S-8, Form 8-K, and Form 20-F by Shell Companies*, Release No. 33-8587 (July 15, 2005) [70 FR 42233] (adopting definition of shell company).

under new General Instruction I.B.6. of Form S-3 on having a class of common equity securities listed and registered on a national securities exchange (often described as "listed" securities).<sup>41</sup>

As proposed, new General Instruction I.B.6. of Form S-3 would have limited the amount of securities eligible companies could sell in accordance with its provisions to no more than the equivalent of 20% of their public float over any period of 12 calendar months. We proposed a cap of 20% in order to allow an offering that is large enough to help an issuer obtain financing when market opportunities arise, yet small enough to take into account the effect such new issuance may have on the market for a thinly traded security. As we stated in the Proposing Release, we believed that the 20% ceiling would help a large number of smaller public companies with their capital raising.<sup>42</sup>

Some commenters, however, were critical of this proposed restriction and concerned that capping issuers at 20% of the value of their public float every twelve months would limit the usefulness of the rule.<sup>43</sup> The commenters thought that the 20% ceiling would be of limited utility because they believed that the capital needs of small businesses would, in many cases, greatly exceed the amount of securities that could be sold under the rule.<sup>44</sup> Several commenters also suggested various alternatives to a 20% limit,<sup>45</sup> including raising the ceiling

<sup>41</sup> New General Instruction I.B.6(c) of Form S-3.

<sup>42</sup> As we noted in the Proposing Release, the Division of Corporation Finance undertook a study of shelf registration takedowns in 2006 by companies with a public float of moderate size in order to evaluate the appropriate public float ceiling for the new rule. Specifically, the Division looked at all prospectus supplements filed pursuant to shelf registration statements in calendar year 2006 by companies with a public float between \$75 million and \$140 million. While we observed a wide range of variously sized shelf takedowns (from less than 1% of float to greater than 80% of float), the data indicated that 20% of float was approximately the median annual takedown for companies in the band considered. This suggested that limiting smaller public companies to 20% of their public float in any 12-month period might increase the capital raising alternatives for these companies consistent with investor protection.

<sup>43</sup> See, for example, letters from the ABA; SBA; Feldman Weinstein; Malizia Spidi; Morrison & Foerster; M. Shichtman; and Roth Capital.

<sup>44</sup> See letters from the SBA; Brinson Patrick; Feldman Weinstein; Malizia Spidi; M. Shichtman; and Roth Capital. For an opposing viewpoint, see letter from the CII.

<sup>45</sup> See, for example, letters from Feldman Weinstein; Morrison & Foerster; and Williams Securities (commenters suggesting that a percentage of trading volume be used as an alternative to public float); Malizia Spidi and Roth Capital (commenters suggesting that shareholder approval be obtained for dilutive issuances constituting over 20% of public float); and letters from Feldman Weinstein and Morrison & Foerster (commenters

from 20% to at least one-third of a company's public float.<sup>46</sup>

After considering these comments, we have decided to set the twelve-month offering threshold under new General Instruction I.B.6. of Form S-3 at one-third of an issuer's public float. We are comfortable making this adjustment in light of the additional protection afforded by the new requirement in General Instruction I.B.6(c) of Form S-3 that eligibility under this instruction is contingent upon the registrant having a class of common equity securities listed and registered on a national

suggesting that additional disclosure be required in lieu of imposing a 20% ceiling). Some commenters were also concerned that the Commission might amend Rule 430B of the Securities Act to vary the application of Section 11 liability to the various parties involved in a shelf registration statement based on the size of the issuer. See letters from BDO Seidman, LLP; Center for Audit Quality; Deloitte & Touche LLP; Ernst & Young LLP ("Ernst & Young"); and KPMG LLP ("KPMG"). These commenters maintained that the filing of a prospectus supplement to a shelf registration statement should not be considered a new effective date for purposes of Section 11 liability for auditors, regardless of the size of the issuer's public float. The set of comprehensive amendments in 2005, known as "Securities Offering Reform," provide in Rule 430B that the effective date for auditors who previously provided consent in an existing registration statement for their report on previously issued financial statements or previous reports on management's assessment of internal control over financial reporting does not change upon the filing of a prospectus supplement unless the prospectus supplement (and any Exchange Act report incorporated by reference into the prospectus and registration statement) contains new audited financial statements or other information as to which the auditor is an expert and for which a new consent is required. Release No. 33-8591. Two of the commenters emphasized that taking a different approach for smaller issuers would run the risk of creating substantial delays in the filing process (as auditors would have to provide new consents) and issuers would likely lose a substantial amount of flexibility in accessing the public markets. See letters from Ernst & Young and KPMG. We agree with these commenters and are not modifying Rule 430B in connection with this rulemaking.

<sup>46</sup> See letters from the ABA; Feldman Weinstein; Morrison & Foerster; M. Shichtman; and Williams Securities. The SBA also suggested raising the threshold in its letter, but did not specify the size of the increase it favored. We note that some of the commenters who advocated increasing the threshold to one-third of a company's public float reasoned that doing so would harmonize the amount of securities which could be registered in a primary offering on Forms S-3 and F-3 under the proposed rule with a purported staff position in a different context. See letter from Feldman Weinstein. See also letters from Morrison & Foerster and Williams Securities. The purported staff position is not related to the instant Form S-3 and Form F-3 amendments, which concern expanding the availability of these forms for primary offerings to more companies. Rather, the staff has indicated that some resale registration statements may raise a concern where, among other things, there is an unusually large number of shares being registered in relation to the number of the issuer's outstanding shares held by nonaffiliates. In these situations, the staff may question whether the offering is a bona fide secondary transaction or a disguised primary offering.

securities exchange, as discussed below. We think raising the cap to one-third of public float will allow an offering that is large enough to help an issuer raise a relatively significant amount of capital when market opportunities arise, but still small enough for us to moderate the expansion of shelf eligibility with appropriate attention to the protection of investors, including the effect such new issuance may have on the market for a thinly traded security.

Under these amendments, offerings above the one-third cap would violate the form requirements of Form S-3. In order to provide absolute clarity on this point, we are adopting a corresponding amendment to Rule 401(g)<sup>47</sup> of the Securities Act to provide that violations of the one-third cap would also violate the requirements as to proper form under Rule 401 even though the registration statement previously has been declared effective.<sup>48</sup>

Our objective with this rulemaking is to provide smaller companies some additional financing flexibility that will aid them in their efforts to raise capital, but at the same time give the Commission an opportunity to consider the impact of this expansion in an environment where there are limitations in place to address investor protection. As a general proposition, the greater the magnitude of the offering, the more likely it is that the transaction will be transformative to the issuer rather than routine in nature, such as the incremental expansion of the issuer's business. At the current time, we believe that securities transactions exceeding one-third of the value of an issuer's public float are generally of such significance to the issuer that the opportunity for specific staff review of the transaction and a greater window for underwriter due diligence are advisable.

We believe that the one-third cap will help a substantial number of smaller public companies with their capital raising needs, which is supported by our observations of market activity of recent shelf registrants.<sup>49</sup> Moreover, it is important to understand that the one-third cap imposed by new General

Instruction I.B.6. to Form S-3 only relates to other primary offerings conducted pursuant to this instruction. Accordingly, an issuer that is temporarily prevented from utilizing Form S-3 for shelf offerings to raise capital would not be foreclosed from registering a primary offering of securities on Form S-1 or in private placements. The new eligibility instruction that we are adopting today is not meant to be mutually exclusive. Rather, it is designed to provide added flexibility to smaller public companies by giving them supplemental avenues of capital formation. As we have stated previously, our adoption of this amendment does not foreclose the possibility that we may revisit the appropriateness of this one-third cap at a later time. For now, however, we think that this limitation promotes small business capital formation consistent with the protection of investors.

At the same time that we are adopting an offering ceiling under new General Instruction I.B.6. of one-third of an issuer's public float, we are also making eligibility under this new rule contingent on the issuer having a class of common equity securities listed and registered on a national securities exchange.<sup>50</sup> In the Proposing Release, we requested comment as to whether we should allow all companies with a public trading market, including companies with securities traded in the over-the-counter market such as the Pink Sheets, to use the amended Form S-3 as proposed or whether we should limit eligibility to inter-dealer quotations systems with some level of oversight and operated by a self-regulatory organization.<sup>51</sup> In addition, we asked whether there were other restraints on the proposed expansion of Form S-3 eligibility that should be considered, such as restrictions on the class of issuers that could utilize the revised forms.<sup>52</sup> Most commenters did not address these specific points directly, but their responses generally suggested that they would not favor further restrictions on a registrant's form eligibility in addition to those already proposed.<sup>53</sup> However, one commenter expressed concern over the risks inherent in expanding the base of companies eligible for primary offerings on Forms S-3 and F-3 and, accordingly, recommended that Form S-3 and Form F-3 eligibility be contingent on full

implementation of both the management and auditor attestation report requirements of Section 404.<sup>54</sup> At a minimum, the commenter opposed any weakening of the proposed limitations on eligibility in the final rule.

Allowing only companies with at least one class of listed common equity securities to avail themselves of new General Instruction I.B.6. should help to minimize potential abuses that may arise from expanded shelf registration. This is because the exchanges' listing rules and procedures, as well as other requirements, provide an additional measure of protection for investors.<sup>55</sup> Exchanges have both quantitative and qualitative listing rules that are designed to evidence that their listed issuers meet specified minimum requirements when the issuer first lists on the exchange and thereafter. Initial listing standards serve as a means for an exchange to screen issuers and to provide listed status to issuers with sufficient public float, investor base, and trading interest to assure that the market for the issuer's security has the depth and liquidity necessary to maintain fair and orderly markets. Maintenance listing criteria help assure that the issuer continues to meet the exchange's standards for depth and liquidity. While the exchanges' listing standards with respect to common equity securities can vary,<sup>56</sup> generally the exchanges require the issuer to meet minimum standards relating to number of public shareholders and shares outstanding, shareholder approval of specified matters, and, in certain cases, earnings or income. Moreover, the exchanges' listing standards generally require issuers of common equity securities to meet strong corporate governance standards, including the requirement that the issuer's board be composed of a majority of independent directors and that key committees be composed solely of independent directors.<sup>57</sup> Exchange-listed securities

<sup>54</sup> See letter from the CII. See also nn. 29 and 31 discussing this letter.

<sup>55</sup> In contrast to the national securities exchanges, automated inter-dealer quotation systems such as the Over-the-Counter Bulletin Board and the Pink Sheets do not provide companies with the ability to list their securities, but, rather, serve as a medium for the over-the-counter securities market by collecting and distributing market maker quotes to subscribers. These automated inter-dealer quotation systems do not maintain or impose listing standards, nor do they have a listing agreement or arrangement with the companies whose securities are quoted through them.

<sup>56</sup> See, for example, Nasdaq Rules 4300 *et seq.*, and NYSE Listed Company Manual ("LCM"), Sections 1 through 9.

<sup>57</sup> See, for example, Nasdaq Rule 4350 and NYSE LCM Section 3, which require listed issuers to

<sup>47</sup> 17 CFR 230.401(g).

<sup>48</sup> See letter from the ABA (recommending that the Commission not revise current Rule 401(g) to provide that an issuer will be deemed to have used an incorrect registration form if it exceeds the one-third cap under new General Instruction I.B.6.).

<sup>49</sup> When we further narrowed the set of shelf registration takedowns reviewed (the original review is referenced in n. 42) to companies with at least one class of listed common equity, the data indicated that 75% of sample registrants took down the equivalent of one-third or less of their public float annually off the shelf. For the majority of these sample registrants, therefore, an offering ceiling of one-third would appear satisfactory.

<sup>50</sup> New General Instruction I.B.6(c) of Form S-3.

<sup>51</sup> The Proposing Release, at 35127.

<sup>52</sup> *Id.*

<sup>53</sup> See, for example, letters from the ABA; Feldman Weinstein; Malizia Spidi; Morrison & Foerster; SBA; M. Shichtman; and Williams Securities.

also are subject to real-time reporting of quotation and transaction information, which benefits investors by apprising them of current market information about the security. Together, these common attributes allow the exchanges to sustain efficient and liquid markets that should help monitor the expansion of shelf registration eligibility on Form S-3 and help mitigate any attendant risks posed by expansion.<sup>58</sup>

We also note that limiting eligibility under new General Instruction I.B.6. to companies with common equity securities listed on a national securities exchange is more consistent with our historical treatment of secondary offering eligibility on Form S-3.<sup>59</sup> We think this parallel approach is sensible given that Form S-3 has for many years allowed registrants to conduct secondary offerings on the form irrespective of public float, so long as the securities offered thereby were listed securities.<sup>60</sup>

Some commenters noted that, under the proposed amendments, companies with securities not listed or authorized for listing on a national securities exchange would nevertheless be eligible to offer such securities in primary offerings on Form S-3 or Form F-3 so long as there was a public trading market for their securities.<sup>61</sup> Because such securities would not be "covered securities," as defined by Section 18(b) of the Securities Act, commenters expressed concern that some companies registering transactions under new General Instruction I.B.6. might well be subject to state securities registration

comply with Rule 10A-3 under the Exchange Act, 17 CFR 240.10A-3, with regard to audit committee responsibility and independence, as well as an additional, broader array of corporate governance standards.

<sup>58</sup> See n. 28.

<sup>59</sup> See General Instruction I.B.3. of Form S-3.

<sup>60</sup> In its comment letter, the ABA pointed out that, as proposed, the eligibility standards for primary offerings on Form S-3 would have allowed both "listed and unlisted" reporting companies to make primary offerings on the form, while resale transactions on Form S-3 are limited to reporting companies whose securities are listed on a national securities exchange or quoted on the automated quotation system of a national securities association. In addition, the ABA noted that the staff of the Commission, through interpretive guidance, has historically permitted unlisted companies that are primarily eligible to use Form S-3 under the existing rules to register resale transactions on Form S-3 notwithstanding that the resale eligibility rules of Form S-3 require that the securities be listed on an exchange or quoted on the automated quotation system of a national securities association. We believe that the final rules, by limiting primary offering eligibility under new General Instruction I.B.6. to companies with equity securities listed on a national securities exchange, address these inconsistencies noted by the ABA in its comment letter.

<sup>61</sup> See letters from the ABA; Feldman Weinstein; Morrison & Foerster; and Williams Securities Law.

requirements, which would frustrate the speed and efficacy of shelf registration. However, because we are limiting eligibility under the new rules to companies with listed equity, in most cases issuers will not be subject to state securities registration requirements in their efforts to raise capital utilizing new General Instruction I.B.6. By requiring issuers to have at least one listed class of common equity securities, most securities offered pursuant to the new eligibility rules will be "covered securities," as defined by Section 18(b) of the Securities Act, and therefore exempt from state Blue Sky regulation.<sup>62</sup>

## 2. Calculation of Amount of Securities That May Be Sold

To ascertain the amount of securities that may be sold pursuant to Form S-3 by registrants with a public float below \$75 million, the new rule requires a two-step process:

- Determination of the registrant's public float immediately prior to the intended sale; and
  - Aggregation of all sales of the registrant's securities pursuant to primary offerings under General Instruction I.B.6. of Form S-3 in the previous 12-month period (including the intended sale) to determine whether the one-third cap would be exceeded.
- The new rule requires registrants to compute their public float by reference to the price at which their common equity was last sold, or the average of the bid and asked prices of their common equity, in the principal market for the common equity as of a date within 60 days prior to the date of sale.<sup>63</sup> Then, for purposes of calculating the aggregate market value of securities sold during the preceding period of 12 calendar months, the rule requires registrants to add together the gross sales price for all primary offerings pursuant to new General Instruction I.B.6. to Form S-3 during the preceding period of 12 calendar months. Based on that calculation, registrants will be permitted to sell securities with a value up to, but not greater than, the difference between one-third of their public float and the value of securities

<sup>62</sup> The exception would be a class of securities that are neither listed nor at least equal in seniority to a class of the issuer's listed securities. See Section 18(b)(1)(A) through (C) of the Securities Act [15 U.S.C. 77r(b)(1) (A) through (C)].

<sup>63</sup> Instruction 1 to new General Instruction I.B.6. of Form S-3. This is modeled after the calculation of public float provided in the instruction to General Instruction I.B.1. of Form S-3. However, the relevant date for purposes of Instruction 1 to new General Instruction I.B.6. is the date of sale, while the relevant date for purposes of General Instruction I.B.1. is the date of filing.

sold in primary offerings on Form S-3 under new General Instruction I.B.6. in the prior period of 12 calendar months.

The aggregate gross sales price includes sales of equity as well as debt offerings.<sup>64</sup> Therefore, eligible registrants will also be able to offer non-investment grade debt on Form S-3.<sup>65</sup> In the case of securities that are convertible into or exercisable for equity shares, such as convertible debt or warrants, however, we are requiring that registrants calculate the amount of securities they may sell in any period of 12 calendar months by reference to the aggregate market value of the underlying equity shares in lieu of the market value of the convertible securities. The aggregate market value of the underlying equity will be based on the maximum number of shares into which the securities sold in the prior period of 12 calendar months are convertible as of a date within 60 days prior to the date of sale, multiplied by the same per share market price of the registrant's equity used for purposes of calculating its public float pursuant to Instruction 1 to new General Instruction I.B.6. of Form S-3. We believe calculating the one-third cap based on the market value of the underlying securities makes it less likely that convertible securities would be structured and offered in a manner designed to avoid the effectiveness of the cap.

It is important to note that the one-third cap on sales is not intended to impact a holder's ability to convert or exercise derivative securities purchased from the company. For example, this limit will apply to the amount of common stock warrants that a company can sell under Form S-3, and the number of common shares into which the warrants are exercisable will be relevant for determining the company's compliance with the one-third cap at the time the warrants were sold, but the number will not impede the purchaser's later exercise of the warrants.

As adopted, the one-third cap is designed to allow issuers flexibility. Because the restriction on the amount of

<sup>64</sup> As adopted, the method of calculating the one-third cap on sales is the same whether the registrant is selling equity or debt securities, or a combination of both. As we discussed in the Proposing Release, we had some concern that we would be inadvertently encouraging issuances of debt securities over equity if the proposed limitation on sales excluded debt. Because we do not intend for the rule to dictate or otherwise influence the overall form of security that companies offer, we have adopted the one-third cap on sales to include both equity and debt.

<sup>65</sup> The provisions of Form S-3 in effect today allow registrants to offer non-convertible investment grade debt securities on Form S-3 regardless of the size of their public float. General Instruction I.B.2. to Form S-3.

securities that can be sold over a period of 12 calendar months is calculated by reference to a registrant's public float immediately prior to a contemplated sale, as opposed to the time of the initial filing of the registration statement, the amount of securities that an issuer is permitted to sell can continue to grow over time as the issuer's public float increases. Therefore, the value of one-third of a registrant's float during the period that a shelf registration statement is effective may, at any given time, be much greater than at the time the registration statement was initially filed. Registrants may therefore benefit from increases in the size of their public float during the time that the registration statement is effective. Conversely, the amount of securities that an issuer is permitted to sell at any given time may also decrease if the issuer's public float contracts. It is important to note, however, that a contraction in a registrant's float, such that the value of one-third of the float decreases from the time the registration statement was initially filed, would not necessarily run afoul of the cap because the relevant point in time for determining whether a registrant has exceeded the threshold is the time of sale. If the sale of securities, together with all securities sold in the preceding period of 12 calendar months, does not exceed one-third of the registrant's float calculated within 60 days of the sale, then the transaction would not violate new General Instruction I.B.6. to Form S-3 even if the registrant's public float later drops to a level such that the prior sale now accounts for over one-third of the new lower float.<sup>66</sup> To keep track of the securities sold under General Instruction I.B.6., the revised instructions to Form S-3 require registrants to disclose in each prospectus filed with the Commission their updated calculation of public float and the amount of securities offered pursuant to this instruction during the prior 12 calendar month period that

<sup>66</sup> Along these lines, under the amendments registrants will be able to sell up to the equivalent of the full one-third of their public float immediately following the effective date of their registration statement, provided that there were no prior sales pursuant to new General Instruction I.B.6. of Form S-3. This is consistent with Rule 415(a)(1)(x), which was amended in 2005 to allow primary offerings on Form S-3 or Form F-3 to occur immediately after effectiveness of a shelf registration statement. Release No. 33-8591. Assuming that the sale of the entire one-third of public float allotted under the new form eligibility rules complied with the rule at the time of the takedown, the subsequent contraction in the registrant's public float will not invalidate this prior sale.

ends on, and includes, the date of the prospectus.<sup>67</sup>

Because Form S-3 registrants who meet the \$75 million float threshold of existing General Instruction I.B.1. at the time their registration statement is filed are not subject to restrictions on the amount of securities they may sell under the registration statement even if their float falls below \$75 million subsequent to the effective date of the Form S-3 but prior to the update required under Section 10(a)(3) of the Securities Act, we believe it is appropriate to provide issuers registering on Form S-3 pursuant to new General Instruction I.B.6. the same flexibility if their float increases to a level that equals or exceeds \$75 million subsequent to the effective date of their Form S-3 without the additional burden of filing a new Form S-3 registration statement. Therefore, we are adopting an instruction to I.B.6. that lifts the one-third cap on additional sales in the event that the registrant's float increases to \$75 million or more subsequent to the effective date of the registration statement.<sup>68</sup> Of course, pursuant to Rule 401 under the Securities Act, registrants are also required to recompute their public float each time an amendment to the Form S-3 is filed for the purpose of updating the registration statement in accordance with Section 10(a)(3) of the Securities Act—typically when an annual report on Form 10-K is filed. In the event that the registrant's public float as of the date of the filing of the annual report is less than \$75 million, the one-third cap will be reimposed for all subsequent sales made pursuant to new General Instruction I.B.6. and will remain in place until the registrant's float equals or exceeds \$75 million.

The following examples illustrate how the new Instruction will operate.<sup>69</sup> For purposes of these examples, we are assuming that the hypothetical registrants satisfy the registrant eligibility requirements in General Instruction I.A. of Form S-3, are not shell companies, and have at least one class of common equity securities listed and registered on a national securities exchange.

#### Example A

On January 1, 2009, a registrant with a public float of \$25 million files a shelf registration statement on Form S-3 pursuant to new General Instruction I.B.6. intending to register the offer and

<sup>67</sup> Instruction 7 to new General Instruction I.B.6.

<sup>68</sup> Instruction 3 to new General Instruction I.B.6. of Form S-3.

<sup>69</sup> The examples that follow are for illustrative purposes only and are not intended to be indicative of actual market activity.

sale of up to \$50 million of debt and equity securities over the next three years from time to time as market opportunities arise.<sup>70</sup> The registration statement is subsequently declared effective. In March 2009, the registrant decides to sell common stock off the registration statement. To determine the amount of securities that it may sell in connection with the intended takedown, the registrant calculates its public float as of a date within 60 days prior to the anticipated date of sale, pursuant to Instruction 1 to new General Instruction I.B.6. Calculating that its public float has risen to \$30 million, the registrant determines that the total market value of all sales effected pursuant to new General Instruction I.B.6. over the past year, including the intended sale, may not exceed \$10 million, or one-third of the registrant's float. Since the registrant has conducted no prior securities offerings on Form S-3 pursuant to new General Instruction I.B.6., it is able to sell the entire \$10 million off the Form S-3.

Assuming that it sold the entire \$10 million of securities in March 2009, the registrant in September 2009 once again contemplates a takedown off the shelf. It determines that its public float (as calculated pursuant to Instruction 1 to new General Instruction I.B.6.) has again risen, this time to \$54 million. Because one-third of \$54 million is \$18 million, the registrant is now able to sell additional securities in accordance with new General Instruction I.B.6(a), even though in March 2009 it took down the equivalent of what was then the entire one-third of its float. However, because the registrant has already sold \$10 million worth of its securities within the 12 calendar months prior to the contemplated sale, the registrant may sell no more than \$8 million of additional securities at this time (\$18 million minus \$10 million of securities previously sold).

In December 2009, the registrant determines that its public float has risen to \$78 million. To this point, assuming it has only sold an aggregate of \$18 million of its securities pursuant to the subject Form S-3 as described above, it has \$32 million of securities remaining on the registration statement and potentially available for takedown (the total amount registered of \$50 million, less the \$18 million previously sold).

<sup>70</sup> Although only one-third of the public float may be sold in any year, a company may register a larger amount. Release No. 33-8591 at 44774-5 (discussing the adoption of an amendment to Rule 415 that eliminated limits on the amount of securities that may be registered on Form S-3 or Form F-3 under Rule 415(a)(1)(x) and Rule 415(a)(1)(ix)).

Because one-third of \$78 million is \$26 million, and the registrant has already sold \$18 million within the previous year, new General Instruction I.B.6(a) will, in most circumstances, prohibit the registrant from selling more than an additional \$8 million of securities in the latest offering. However, under Instruction 3 to new General Instruction I.B.6., the registrant is no longer subject to the one-third cap on annual sales because its float has exceeded \$75 million. If it chooses, the registrant may sell the entire \$32 million of securities remaining on the registration statement all at once or in separate tranches at any time until the company next updates the registration statement pursuant to Section 10(a)(3) by filing its Form 10-K. This will be the case even if the registrant's float subsequently falls below \$75 million before it files that Form 10-K, at which time the registrant is required to recompute its public float in accordance with Rule 401. In the event that the registrant's public float as of the date of that Form 10-K filing is less than \$75 million, the one-third cap will be reimposed for all subsequent sales made pursuant to new General Instruction I.B.6. and will remain in place until the registrant's float equals or exceeds \$75 million.

#### Example B

A registrant has 12 million shares of voting common equity outstanding held by nonaffiliates. The market price of this stock is \$5 per share, so the registrant has a public float of \$60 million. The registrant has an effective Form S-3 shelf registration statement filed in reliance on new General Instruction I.B.6. of Form S-3, pursuant to which the registrant wants to issue \$10 million of convertible debt securities which will be convertible into common stock at a 10% discount to the market price of the common stock. Pursuant to Instruction 2 to new General Instruction I.B.6., the amount of securities issued is measured by reference to the value of the underlying common stock rather than the amount for which the debt securities will be sold. At the 10% discount, the conversion price is \$4.50 and, as a result, 2,222,222 shares currently underlie the \$10 million of convertible debt. Because the current market price of those underlying shares is \$5 per share, for purposes of General Instruction I.B.6. the value of the securities being offered is \$11,111,110 (2,222,222 shares at \$5 per share), which is less than the \$20 million allowed by the one-third cap (one-third of \$60 million).

After the convertible debt securities are sold and are outstanding, the

registrant contemplates an additional takedown. To determine the amount of securities that the registrant may sell under General Instruction I.B.6. in the anticipated offering, the registrant must know its current public float and must calculate the aggregate market value of all securities sold in the last year on Form S-3 pursuant to General Instruction I.B.6. Instruction 2 to new General Instruction I.B.6. requires that the registrant compute the market value of convertible debt securities sold under I.B.6. by reference to the value of the underlying common stock rather than the amount for which the debt securities were sold. With respect to the notes that were sold and have been converted, the aggregate market value of the underlying common stock is calculated by multiplying the number of common shares into which the outstanding convertible securities were converted times the market price on the day of conversion. With respect to the notes that were sold but have not yet been converted, the aggregate market value of the underlying common stock is calculated by multiplying the maximum number of common shares into which the notes are convertible as of a date within 60 days prior to the anticipated sale by the per share market price of the registrant's equity used for purposes of determining its current float.<sup>71</sup>

In this example, assume that the registrant has a current per share stock price of \$5.55. If half of the notes converted into common stock while the per share market price was \$5.00 (\$4.50 discount), then, for purposes of Instruction 2 to new General Instruction I.B.6., the value of that prior issuance is \$5,555,555 (half of the notes divided by the discounted conversion price of \$4.50 and then multiplied by \$5, the market price on the day of conversion).

As for the notes that have not yet been converted, the aggregate market value of the underlying common stock is determined by calculating the number of shares that may be received upon conversion and multiplying that by the current market value of \$5.55. Therefore, the outstanding note amount (\$5 million) is divided by the discount conversion price (\$5), resulting in 1,000,000 shares and this amount is then multiplied by the current market value of \$5.55. Thus, for purposes of Instruction 2 to new General Instruction

<sup>71</sup> The date chosen by the registrant for determination of the maximum number of shares underlying the convertible notes must be the same date that the registrant chooses for determining its market price in connection with the calculation of public float pursuant to new General Instruction I.B.6. See Instruction 5 to new General Instruction I.B.6.

I.B.6., \$5,550,000 is the value of the outstanding notes that have not yet been converted. Adding this to the value of the notes that have already been converted results in a total value of \$11,105,555 having been issued under this Form S-3.

To determine the amount of additional securities that the registrant may sell under General Instruction I.B.6., the registrant should add the value of the notes issued (\$11,105,555) plus the value of all other securities sold by the registrant pursuant to Instruction I.B.6. during the preceding 12 calendar months. If this amount is less than one-third of the registrant's current public float, it may sell additional securities with a value up to, but not greater than, the difference between one-third of its current public float and the value of all securities sold by it pursuant to Instruction I.B.6. during the preceding 12 calendar months.

#### Example C

A registrant has an effective registration statement on Form S-3, filed pursuant to new General Instruction I.B.6., through which it intends to conduct shelf offerings of its securities. At the time of its first shelf takedown, the registrant's public float is equal to \$21 million (which means that the maximum amount available to be sold under the one-third cap would be \$7 million). Based on new General Instruction I.B.6(a), the registrant sells \$3 million of its debt securities. Six months later, the registrant's public float has decreased to \$9 million. The registrant wishes to conduct an additional takedown of debt securities off the shelf but, because of the reduction in its float, it is prohibited from doing so. This is because with a public float of \$9 million, General Instruction I.B.6(a) only allows the registrant to sell a maximum of \$3 million worth of securities (one-third of \$9 million) pursuant to the registration statement during the prior period of 12 calendar months that ends on the date of the contemplated sale. However, the registrant has already sold securities valued (for purposes of new General Instruction I.B.6.) at \$3 million in the 6 months prior to the contemplated sale and so must wait until at least one full year has passed since the \$3 million sale of securities to undertake another offering off the Form S-3 unless its float increases. Note that although the registrant's float does not allow additional sales, the \$3 million takedown of securities 6 months prior does not violate the one-third cap because, at the time of that prior sale, the registrant's float was \$21 million.

*Example D*

Pursuant to new General Instruction I.B.6., a registrant with a public float of \$48 million files a Form S-3, which the registrant intends to use as a universal shelf registration statement to sell up to \$100 million of debt or equity securities, or a combination of both at any time or from time to time.

After the registration statement is declared effective, the registrant decides to do a takedown off the shelf comprised of convertible promissory notes and warrants to purchase to common stock. The notes are convertible into shares of common stock at a 50% discount to the market price of the common stock. The warrants are exercisable for shares of common stock at an exercise price equal to \$5 per share. Because the registrant's float is \$48 million, it may sell up to \$16 million of securities (one-third of \$48 million) pursuant to General Instruction I.B.6. The registrant wants to do a takedown of \$1 million in convertible promissory notes. The registrant intends to issue the notes along with warrants to purchase an additional 10,000 shares of its common stock.

In order to determine if this sale is permissible under General Instruction I.B.6., the registrant must calculate the amount of securities it has sold pursuant to General Instruction I.B.6. in the previous 12 months and add this to the value of the securities in the intended sale. If the combined value is \$16 million or less, it may proceed with the sale.

Assume that the registrant has not sold any securities pursuant to the Instruction I.B.6. in the previous 12 months. To determine the value of the convertible promissory notes, the registrant is required by Instruction 2 to General Instruction I.B.6. to calculate the value of the shares underlying the convertible notes. The notes are convertible into shares of common stock at a 50% discount to the market price of the common stock. Assuming that the market price of the common stock is \$2 per share, the notes are convertible as follows: \$1 million (the price of the notes) divided by 1 (50% of the market price of the common stock) is equal to 1 million shares of common stock that the purchasers will receive upon conversion. Since the market price of the stock is \$2 per share, the value of the 1 million shares is \$2 million (1 million shares at \$2 per share). Therefore, the value of the accompanying warrants for 10,000 shares must be less than \$14 million for the sale to be within the one-third cap (one-third of \$48 million, less the \$2

million of common stock underlying the convertible notes).

To calculate the value of the warrants, which are derivative securities, Instruction 2 to General Instruction I.B.6. requires that the registrant calculate the value of the shares underlying the warrants in lieu of the market value of the warrants. Under the terms of the warrants, the warrants are exercisable for 10,000 shares at an exercise price of \$5 per share.

Instruction 2 to General Instruction I.B.6. states that the aggregate market value of the underlying equity shall be calculated by multiplying the maximum number of common equity shares into which the derivative securities are convertible or for which they are exercisable, as of a date within 60 days prior to the date of sale, by the same per share market price of the registrant's equity used for purposes of calculating the registrant's float. Assuming that the market price of the registrant's stock is \$2 per share, the value of the shares underlying the warrants is \$20,000 (10,000 shares multiplied by \$2 per share). Because the underlying value of the convertible notes is \$2 million and the underlying value of the warrants is \$20,000, the intended sale has a value of \$2,020,000 and does not exceed the one-third cap (of \$16 million).

### 3. Exclusion of Shell Companies

In accordance with our desire to expand Form S-3 eligibility consistent with the protection of investors, the expanded eligibility rules specifically exclude shell companies, which will be prohibited from registering securities in primary offerings on Form S-3 unless they meet the minimum \$75 million float threshold of General Instruction I.B.1.<sup>72</sup> While we are not passing on the relative merits of shell companies and we recognize that these entities are used for many legitimate business purposes, we have repeatedly stated our belief that these entities may give rise to disclosure abuses.<sup>73</sup> Under the final rules, a former

<sup>72</sup> This prohibition is intended to apply equally to "blank check companies," as such entities are defined in Rule 419 of the Securities Act. However, because we believe that the definition of "shell company" under Rule 405 is expansive enough to encompass blank check companies for purposes of excluding them from S-3 eligibility under new General Instruction I.B.6., we do not exclude them separately. See *Use of Form S-8 and Form 8-K by Shell Companies*, Release No. 33-8407 (Apr. 15, 2004) [69 FR 21650], at n. 20.

We believe that under today's proposals all blank check companies as defined in Rule 419 would be considered shell companies until they acquire an operating business or more than nominal assets. Not all shell companies, however, would be classified as blank check companies under Rule 419.

<sup>73</sup> See, for example, Release No. 33-8591; Release No. 33-8587; Release No. 33-7393; and *Penny*

shell company that cannot meet the \$75 million float criterion but otherwise satisfies the registrant requirements of Form S-3 will become eligible to use Form S-3 to register primary offerings of its securities, provided that:

- It has not been a shell company for at least 12 calendar months;<sup>74</sup>
- It has filed information that would be required in a registration statement on Form 10 or Form 20-F, as applicable, to register a class of securities under Section 12 of the Exchange Act;<sup>75</sup> and
- It has been timely reporting for 12 calendar months.<sup>76</sup>

Ordinarily, the information required to be filed would be in a current report on Form 8-K, reporting completion of the transaction that caused it to cease being a shell company.<sup>77</sup> In other cases, the information may be filed in a Form 10 or Form 20-F. Consistent with the current registrant eligibility rules of Form S-3 that require at least 12 calendar months of timely reporting, the 12 calendar-month delay under the new rules is intended to provide investors in the former shell company with the benefit of disclosure over a full 12-month period in the newly structured entity prior to its use of Form S-3 for primary securities offerings.

Commenters held contrasting opinions of our proposal to exclude shell companies<sup>78</sup> and the requirement that former shell companies may not rely on General Instruction I.B.6. to

*Stock Definition for Purposes of Blank Check Rule*, Release No. 33-7024 (Oct. 25, 1993) [58 FR 58099].

<sup>74</sup> Similarly, Form S-8 is not available to shell companies or to former shell companies until 60 days after they have ceased being shell companies and have filed information that would be required in a registration statement on Form 10 or Form 20-F, as applicable, to register a class of securities under Section 12 of the Exchange Act. Release No. 33-8587. Unlike the eligibility rules of Form S-8, however, a company must be reporting for at least 12 calendar months before it is eligible under any criteria to use Form S-3. Therefore, instead of the 60-day delay required by Form S-8, it is more appropriate for a shell company to be prohibited from using the new provisions of S-3 and F-3 until at least 12 calendar months after it ceases being a shell company.

<sup>75</sup> This information is collectively described as "Form 10 information." See Instruction 4 to new General Instruction I.B.6(b).

<sup>76</sup> New General Instruction I.B.6(b) of Form S-3 addresses the requirements pertaining to former shell companies.

<sup>77</sup> Items 2.01(f) and 5.01(a)(8) of Form 8-K require a company in a transaction where the company ceases being a shell company to file a current report on Form 8-K containing the information (or identifying the previous filing in which the information is included) that would be required in a registration statement on Form 10 to register a class of securities under Section 12 of the Exchange Act.

<sup>78</sup> See letters from the ABA and Morrison & Foerster (supporting the exclusion of shell companies) and letter from M. Baum (opposing the exclusion).

Form S-3 until at least one year has elapsed since they ceased being shell companies.<sup>79</sup> Because of the limited and less comprehensive public information available regarding shell companies, we are adopting General Instruction I.B.6(b) as proposed to ensure that investors have the benefit of one full year of disclosure once the entity ceases to be a shell company. In this regard, requiring one year of timely reporting puts our treatment of former shell companies on par with the eligibility requirements of any other new company wishing to use Form S-3.<sup>80</sup>

### C. Amendments to Form F-3

Form F-3, which was designed to parallel Form S-3,<sup>81</sup> is the equivalent short-form registration form available for use by “foreign private issuers”<sup>82</sup> to register securities offerings under the Securities Act. Similar to Form S-3, Form F-3 is available to foreign private issuers that satisfy the form’s registrant requirements and at least one of the form’s transaction requirements.<sup>83</sup> The Form F-3 registrant requirements are similar to Form S-3 and generally relate to a registrant’s reporting history under

<sup>79</sup> See letters from the ABA and Morrison & Foerster (supporting the one-year delay) and letters from Feldman Weinstein and Williams Securities (objecting to the one-year delay and contrasting it to the 90-day delay the Commission proposed in Release No. 33-8813 (July 5, 2007) [72 FR 36822] in order for shareholders of former shell companies to resell their securities in reliance on Rule 144). This analogy to Rule 144 is inapposite. A delay of at least 90 days under Rule 144, versus one year under Form S-3, is not unique to shell companies. Form S-3 requires any issuer to have been timely reporting for at least one year, while Rule 144 requires that an issuer be subject to the reporting requirements for at least 90 days before an affiliate of a reporting issuer is able to sell unrestricted securities under the rule.

<sup>80</sup> See General Instruction I.A.3. of Form S-3.

<sup>81</sup> *Integrated Disclosure System for Foreign Private Issuers*, Release No. 33-6360 (Nov. 20, 1981) [46 FR 58511], at 7:

The three forms proposed under the Securities Act roughly parallel proposed Forms S-1, S-2 and S-3 in the domestic integration system, but the foreign system is based on the Form 20-F instead of the Form 10-K and annual report to shareholders as the uniform disclosure package.

<sup>82</sup> The term “foreign private issuer” is defined in Rule 405 of the Securities Act to mean any foreign issuer other than a foreign government except an issuer meeting the following conditions:

(1) More than 50 percent of the outstanding voting securities of such issuer are directly or indirectly owned of record by residents of the United States; and

(2) Any of the following:

(i) The majority of the executive officers or directors are United States citizens or residents;

(ii) More than 50 percent of the assets of the issuer are located in the United States; or

(iii) The business of the issuer is administered principally in the United States.

<sup>83</sup> General Instruction I. of Form F-3: “Eligibility Requirements for Use of Form F-3.”

the Exchange Act.<sup>84</sup> In addition, like the Form S-3 registration statement, Form F-3 limits the ability of registrants to conduct primary offerings on the form unless their public float equals or exceeds a particular threshold.<sup>85</sup>

As with Form S-3, the Commission has attempted to limit the availability of Form F-3 for primary offerings to a class of companies believed to provide a steady stream of corporate disclosure that is broadly disseminated to, and digested by, the marketplace. When the Commission adopted Form F-3 in 1982,<sup>86</sup> it set the public float test for foreign issuers at \$300 million in response to public comment recommending that the numerical test for foreign issuers be much greater than for domestic registrants.<sup>87</sup> In 1994, however, the Commission reduced this threshold to \$75 million in order to extend to foreign issuers the benefits of short-form registration “to the same extent available to domestic companies.”<sup>88</sup> In explaining its rationale, the Commission stated:

[Our] experience with foreign issuers, as well as the internationalization of securities markets, indicates that foreign issuers with a public float of \$75 million or more have a degree of analyst following in their worldwide markets comparable to similarly-sized domestic companies.<sup>89</sup>

As a result, the Commission believed that expanding Form F-3 eligibility by lowering the float standard to \$75 million would give foreign issuers the same capital raising advantages enjoyed

<sup>84</sup> One difference is that, unlike Form S-3, General Instruction I.A.1. of Form F-3 requires that registrants have previously filed at least one annual report on Form 20-F, Form 10-K or, in certain cases, Form 40-F under the Exchange Act. For an explanation of this difference, see *Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports*, Release No. 33-7029 (Nov. 3, 1993) [58 FR 60307], at 3; and *Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports*, Release No. 33-7053 (Apr. 19, 1994) [59 FR 21644], at 2 (explaining that the requirement was adopted “in order to ensure that information regarding the issuer is available to the market”).

<sup>85</sup> General Instruction I.B.1. of Form F-3. Note that, unlike Form S-3, the Instruction makes reference to the registrant’s “worldwide” public float.

<sup>86</sup> *Adoption of Foreign Issuer Integrated Disclosure System*, Release No. 33-6437 (Nov. 19, 1982) [47 FR 54764].

<sup>87</sup> Release No. 33-7029, at 2.

<sup>88</sup> Release No. 33-7053, at 2. In the same rulemaking, the Commission also reduced the reporting history requirement in Form F-3 from 36 to 12 months to match the eligibility criteria applicable to domestic companies using Form S-3.

<sup>89</sup> Release No. 33-7029, at 2.

by domestic issuers on Form S-3 consistent with investor protection.<sup>90</sup>

In order to maintain the rough equivalency between Form S-3 and Form F-3, which have had the same public float criteria for primary offering eligibility since 1994,<sup>91</sup> we are adopting amendments to Form F-3 that are comparable to our changes to Form S-3. Specifically, new General Instruction I.B.5. to Form F-3 will allow foreign private issuers with less than \$75 million in worldwide public float to register primary offerings of their securities on Form F-3, provided:

- They meet the other registrant eligibility conditions for the use of Form F-3;
- The class of securities to be offered is listed and registered on a national securities exchange;
- They do not sell more than the equivalent of one-third of their public float in primary offerings under General Instruction I.B.5. on Form F-3 over any period of 12 calendar months; and
- They are not shell companies and have not been shell companies for at least 12 calendar months before filing the registration statement.

## II. Paperwork Reduction Act

### A. Background

The new rules and amendments to Forms S-3 and F-3 contain “collection of information” requirements within the meaning of the Paperwork Reduction Act of 1995.<sup>92</sup> We published a notice requesting comment on the collection of information requirements in the Proposing Release and submitted these to the Office of Management and Budget for review and approval in accordance with the Paperwork Reduction Act.<sup>93</sup> The titles for the collection of information are:

“Form S-3” (OMB Control No. 3235-0073);

“Form F-3” (OMB Control No. 3235-0256);

<sup>90</sup> The Commission stated:

These provisions are part of the ongoing efforts of the Commission to ease the transition of foreign companies into the U.S. disclosure system, enhance the efficiencies of the registration and reporting processes and lower costs of compliance, where consistent with investor protection.

Release No. 33-7053, at 2.

<sup>91</sup> The Commission’s adoption of the “Securities Offering Reform” amendments in July 2005 is a recent instance where parallel changes were made to Form S-3 and Form F-3. See Release No. 33-8591. For example, the 2005 amendments provided that the ability to conduct an automatic shelf offering under both Form S-3 and Form F-3 is limited to registrants that qualify as “well-known seasoned issuers” under Rule 405 of the Securities Act. We note the minimum public float threshold required to be a well-known seasoned issuer is the same for both Form S-3 and Form F-3.

<sup>92</sup> 44 U.S.C. 3501 *et seq.*

<sup>93</sup> 44 U.S.C. 3507(d) and 5 CFR 1320.11.

“Form S-1”<sup>94</sup> (OMB Control No. 3235-0065); and “Form F-1”<sup>95</sup> (OMB Control No. 3235-0258).

We adopted existing Forms S-3, S-1, F-3 and F-1 pursuant to the Securities Act. These forms set forth the disclosure requirements for registration statements that are prepared by eligible issuers to provide investors with the information they need to make informed investment decisions in registered offerings.

Our amendments to Forms S-3 and F-3 are intended to allow issuers that are ineligible to use Forms S-3 and F-3 for primary offerings because they do not meet the forms’ public float requirements to nevertheless register a limited amount of securities in primary offerings on Form S-3 or Form F-3, as applicable, so long as they are not shell companies, they meet the other eligibility requirements of the forms, and they have at least one class of common equity securities listed and registered on a national securities exchange.

The hours and costs associated with preparing disclosure, filing forms, and retaining records constitute reporting and cost burdens imposed by the collection of information. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

The information collection requirements related to registration statements on Forms S-3, S-1, F-3 and F-1 are mandatory. There is no mandatory retention period for the information disclosed, and the information disclosed would be made publicly available on the EDGAR filing system.

#### B. Summary of Information Collections

Because the amendments that we are adopting in this release pertain principally to Forms S-3 and F-3 eligibility, rather than to the disclosure

required by these forms, we do not believe that the amendments will impose any new recordkeeping or information collection requirements, other than those that will be de minimis in nature.<sup>96</sup> On a per-response basis, therefore, the amendments should not increase or decrease existing disclosure burdens for Form S-3 or Form F-3. However, because we expect that many companies newly eligible for primary offerings on Forms S-3 and F-3 as a result of these amendments will choose to file short-form Form S-3 and Form F-3 registration statements in lieu of Forms S-1 or F-1, as applicable, we believe there will be an aggregate decrease in the disclosure burdens associated with Forms S-1 and F-1 and an increase in the disclosure burdens associated with Forms S-3 and F-3. The shift in aggregate disclosure burden among these forms will be due entirely to the change in the number of annual responses expected with respect to each form, as companies previously ineligible to use Form S-3 and Form F-3 switch to these forms for their public offerings and away from Forms S-1 and F-1.

In addition, because of the anticipated benefits to issuers associated with Forms S-3 and F-3, in particular the lower costs of preparing and filing the registration statements and the ability to make delayed and continuous offerings in response to changing market conditions, we think that this will increase the demand for, and lead to more, company filings on Forms S-3 and F-3 than would otherwise have been made on Forms S-1 and F-1. That is, we think that the opportunity for capital raising will be more robust for many companies because of the availability of shelf registration on Forms S-3 and F-3. We also anticipate that many companies newly eligible to use Forms S-3 or F-3 will choose to offer their securities directly to the public through registration on these

registration forms instead of through private placements and, therefore, we expect comparatively more Forms S-3 and F-3 registration statements to be filed as companies forego private offerings in favor of the public markets.

In order to provide an estimate of the change in the collection of information burden for purposes of the Paperwork Reduction Act, our assumption is that the amendments to Forms S-3 and F-3 will result in an overall increase in the number of such forms filed annually by eligible companies and an overall decrease in the number of Forms S-1 and Forms F-1 filed annually by these companies. As discussed, however, we do not expect that the incremental increase in the number of all Forms S-3 and F-3 filed will be roughly equal to the incremental decrease in the number of Forms S-1 and Forms F-1 filed, because our assumption is that the advantages of shelf registration on Form S-3 and Form F-3 will encourage financings on these forms that would otherwise have been carried out through exempt offerings or perhaps not at all. Therefore, we believe the amendments will result in a net increase in the annual aggregate number of filings on all Forms S-3, S-1, F-3 and F-1 taken together, since the increased number of Form S-3 and F-3 filings should exceed the decreased number of Form S-1 and F-1 filings. Accordingly, we believe the overall net decrease in disclosure burden that should result from companies changing to the more streamlined Forms S-3 and F-3 will be offset to some extent by newly eligible companies filing Forms S-3 and F-3 more frequently than they did Forms S-1 or F-1. However, this offset could be lessened in part by the one-third cap on the amount of securities that eligible companies may sell on Form S-3 and Form F-3 in any period of 12 calendar months pursuant to the new form eligibility rules.<sup>97</sup> Companies that require more capital but are prohibited by this one-third cap from using Form S-3 and Form F-3 for primary offerings may, as a result, continue to conduct some offerings on Forms S-1 or F-1 or through the private markets even though Forms S-3 and F-3 are preferable.

#### C. Summary of Comments and Revisions to Amendments

None of the commenters addressed our request for comment on the Paperwork Reduction Act analysis contained in the Proposing Release. We

<sup>94</sup> Because our amendments to Form S-3 and Form F-3 are anticipated to affect the annual number of Forms S-1 and Forms F-1 filed, we are including them in the titles of information collections even though we are not amending the substance of the collection in this release. Note that the Proposing Release also included our estimates with respect to Form SB-2 (OMB Control No. 3235-0418), in addition to Forms S-3, F-3, S-1 and F-1. However, Release No. 33-8876, which was adopted by the Commission on November 15, 2007, will eliminate Form SB-2 when it becomes effective. Therefore, our revised Paperwork Reduction Act estimates do not include new estimates for Form SB-2. As discussed in greater detail below, we have taken the elimination of Form SB-2 into consideration for purposes of revising our estimates of the burden associated with Forms S-3, S-1 and F-1.

<sup>95</sup> *Id.*

<sup>96</sup> Instruction 7 to new General Instruction I.B.6. of Form S-3 and Instruction 7 to new General Instruction I.B.5. of Form F-3 require registrants to disclose in each prospectus filed with the Commission their updated calculation of public float and the amount of securities offered on Form S-3 or F-3, as applicable, pursuant to this instruction during the prior 12 calendar months. Although this is a new disclosure requirement for Forms S-3 and F-3, we think that the registrant’s determination of its public float and the amount of securities offered in the prior twelve-month period should be readily accessible and easily calculable. In addition, we note that registrants are already required to ascertain their public float at the time they file a registration statement for a primary offering on Form S-3 or Form F-3. See General Instruction I.B.1. of Form S-3 and General Instruction I.B.1. of Form F-3. As such, we anticipate that the total time, effort and financial resources to generate and maintain this information will be insignificant for each registrant.

<sup>97</sup> As previously discussed, new General Instructions I.B.6. of Form S-3 and I.B.5. of Form F-3 prohibit registrants from selling more than the equivalent of one-third of their public float in any period of 12-calendar months.

are nevertheless revising our Paperwork Reduction Act estimates in light of certain modifications we have made to the final rules as opposed to the proposal.

As proposed, new General Instruction I.B.6. of Form S-3 and new General Instruction I.B.5. of Form F-3 would have limited the amount of securities eligible companies could sell in accordance with these provisions to no more than the equivalent of 20% of their public float over any period of 12 calendar months. In consideration of commenters who were concerned that capping issuers at 20% of the value of their public float every twelve months would limit the usefulness of these new rules, we have decided to increase the twelve-month offering threshold to one-third of an issuer's public float. In light of this increase, however, we are adopting a further condition to eligibility under new General Instruction I.B.6. of Form S-3 and new General Instruction I.B.5. of Form F-3 that the issuer must have at least one class of common equity securities listed and registered on a national securities exchange. This additional restriction should help to minimize the potential abuses arising from expanded shelf registration because the securities exchanges, through their listing rules and procedures, as well as other requirements, provide an additional measure of protection for investors.

#### *D. Revised Paperwork Reduction Act Burden Estimates*

As discussed in Section II.C. above, we are revising our Paperwork Reduction Act burden estimates that were originally submitted to the Office of Management and Budget. Our revised estimates reflect the changes that we have made to the final rules as compared to the proposal.

For purposes of the Paperwork Reduction Act, we now estimate the annual decrease in the paperwork burden for companies to comply with our collection of information requirements to be approximately 10,375 hours of in-house company personnel time and to be approximately \$12,450,000 for the services of outside professionals.<sup>98</sup> These estimates include the time and the cost of preparing and reviewing disclosure, filing documents and retaining records. Our methodologies for deriving the above estimates are discussed below.

Our estimates represent the burden for all issuers, both large and small. As

<sup>98</sup> For administrative convenience, the totals related to the paperwork burden hours have been rounded to the nearest whole number and the cost totals have been rounded to the nearest thousand.

mentioned, however, the estimated decreases are wholly attributable to our assumptions, discussed in Section II.B. above, about how the amendments will influence the behavior of certain issuers who were formerly ineligible to conduct primary offerings on Forms S-3 and F-3. These issuers are non-shell companies who satisfy the registrant eligibility requirements of Form S-3<sup>99</sup> or Form F-3,<sup>100</sup> as applicable, have at least one class of common equity securities listed and registered on a national securities exchange, and had a public float of less than \$75 million at the end of their last fiscal year. In all, we estimate that there were approximately 1,400 such companies at the end of calendar year 2006 and that they filed a total of 66 registration statements on Forms S-1, SB-2<sup>101</sup> and F-1 during the twelve months ending December 31, 2006.<sup>102</sup> To determine the effect of our amendments on the overall paperwork burden, we have assumed that these filings on Forms S-1, SB-2<sup>103</sup> and F-1 would be made instead on Form S-3 or Form F-3, as applicable, to the extent that the issuers would not be limited by the one-third cap on the amount of securities they may sell in any period of 12 calendar months under the new rules. Therefore, we assume that the Forms S-1 and F-1 filed by the subject companies will decrease from the number filed in 2006, but because of the one-third cap on sales, will not decrease to 0.<sup>104</sup> Instead, we believe that

<sup>99</sup> See n. 37.

<sup>100</sup> See n. 83.

<sup>101</sup> As mentioned, the Commission voted to eliminate Form SB-2 on November 15, 2007. Release No. 33-8876. However, because some of the companies who filed on Form SB-2 in 2006 will become eligible to use Form S-3 under the new amendments to the form, we factor these Form SB-2 filings into our estimate of the number of additional Forms S-3 that will be filed in 2008 as a result of the rule change.

<sup>102</sup> The total of 66 filings is comprised of 37 Forms S-1; 26 Forms SB-2; and 3 Forms F-1.

<sup>103</sup> See n. 101.

<sup>104</sup> Because it has been eliminated, the number of new Forms SB-2 will, in fact, decrease to 0 after Release No. 33-8876 goes into effect. Therefore, companies that previously filed Forms SB-2, but who are now eligible to use Form S-3 under new General Instruction I.B.6. of the form, would not be able to fall back to Form SB-2 in the event that they exceed the one-third cap on Form S-3. Instead, to the extent they wanted to conduct an additional registered public offering, they would likely have to file on Form S-1. To reflect this, we have taken the number of 2006 Form SB-2 filings by companies that we estimate will become eligible on Form S-3 under the new rules and added this to the number of Forms S-1 filed in 2006 by companies who qualify to use Form S-3 for primary offerings under the new rules. This allows us to estimate how many total Forms S-1 will be filed by domestic companies that exceed the one-third cap but still wish to conduct registered public offerings. So, for purposes of our baseline assumptions, the number of Forms S-1 filed in 2006 by companies who will

some Forms S-1 and F-1 will continue to be filed annually by these companies. To reflect this, we have taken the number of Forms S-1 and F-1 that were filed by these companies in calendar year 2006 and decreased this number by 90%<sup>105</sup> for each form, for a total decrease of 60 filings.<sup>106</sup> Therefore, we assume that approximately 60 fewer Forms S-1 and F-1 will be filed by all issuers annually as a result of the new amendments. The actual number could be more or less depending on various factors, including future market conditions.

Furthermore, we believe that the 1,400 companies that we estimate will be affected by the rule change would have conducted more registered securities offerings had they been able to use Forms S-3 and F-3, because of the benefits of forward incorporation and the ability to utilize shelf registration to maximize market opportunities. We assume that the inability of these companies to utilize Forms S-3 and F-3 limited their capacity to access the public securities markets and, because of the cost and lack of flexibility associated with Forms S-1, SB-2 and F-1, they either did not file registration statements on Forms S-1 SB-2 or F-1, or were limited in the number that they filed. We therefore believe that the annual number of responses on Forms S-3 and F-3 for purposes of the Paperwork Reduction Act will increase by an increment greater than simply the total of 60 fewer registration statements on Forms S-1 and F-1 that we estimate will be filed in future years by the 1,400 companies who would qualify for primary offerings on Forms S-3 and F-3 as a result of our amendments. We further assume that this increase in Forms S-3 and F-3 will be mitigated to some degree by the one-third cap on securities sold in any period of 12 calendar months under the new rules, which may limit the

become eligible to use Form S-3 under the new rules will include the number of Forms SB-2 filed in 2006 by qualifying companies (26) and will therefore total 63 filings (37 Forms S-1 plus 26 Forms SB-2).

<sup>105</sup> In the Proposing Release, this decrease was 85% for each form but has been raised to 90% in light of the 12-month offering restriction on sales being raised from 20% to one-third of a company's public float. In other words, because the ceiling has been raised, eligible companies will be able to expand the size and/or frequency of their offerings on Forms S-3 and F-3 and, consequently, will have less need to file alternate registration forms. Therefore, the number of filings on these forms should decrease even more than was predicted in the Proposing Release.

<sup>106</sup> This number deducts 90% from the totals for each of the registration forms, as follows: Form S-1 (90% of 63, rounded up, equals 57) and Form F-1 (90% of 3, rounded up, equals 3). Adding these together, the combined reduction totals 60 filings.

frequency and volume of additional securities offerings on Form S-3 and Form F-3. To reflect this, we have taken the total of 60 fewer Forms S-1 and F-1 that we think will be filed by these companies in future years as a result of the amendments (because of the availability of Forms S-3 and F-3) and increased this number by 15%<sup>107</sup> for each form, for a total increase of 70 filings.<sup>108</sup> Therefore, we assume that approximately 70 additional Forms S-3 and F-3 will be filed annually over and above the number of total Forms S-3 and F-3 filed by all issuers, large and small, as a result of the new amendments. The actual number could be more or less depending on various

factors, including future market conditions.

To calculate the total effect of the amendments on the overall compliance burden for all issuers, large and small, we subtracted the burden associated with the 60 fewer Forms S-1 and F-1 registration statements that we expect will be filed annually in the future and added the burden associated with our estimate of 70 additional Forms S-3 and F-3 filed annually as a result of the amendments. We used current Office of Management and Budget estimates in our calculation of the hours and cost burden associated with preparing, reviewing and filing each of these forms.

Consistent with current Office of Management and Budget estimates and

recent Commission rulemaking,<sup>109</sup> we estimate that 25% of the burden of preparation of Forms S-3, S-1, F-3 and F-1 is carried by the company internally and that 75% of the burden is carried by outside professionals retained by the issuer at an average cost of \$400 per hour.<sup>110</sup> The portion of the burden carried by outside professionals is reflected as a cost, while the portion of the burden carried by the company internally is reflected in hours.

The table below illustrates our estimates concerning the incremental annual compliance burden in the collection of information in hours and cost for Forms S-3, S-1, F-3 and F-1 as a result of these amendments.

Form	Estimated change in annual responses (A)	Hours/form <sup>111</sup> (B)	Incremental burden (C)=(A)*(B)	25% Issuer (D)=(C)*0.25	75% Professional (E)=(C)*0.75	\$400/hr Professional cost (F)=(E)*\$400
S-3 .....	66	459	30,294	7,573.50	22,720.50	\$9,088,200
S-1 .....	(57)	1,176	(67,032)	(16,758)	(50,274)	(20,109,600)
F-3 .....	4	166	664	166	498	199,200
F-1 .....	(3)	1,809	(5,427)	(1,356.75)	(4,070.25)	(1,628,100)
<b>Total .....</b>			<b>(41,501)</b>	<b>(10,375.25)</b>	<b>(31,125.75)</b>	<b>(\$12,450,300)</b>

**III. Cost-Benefit Analysis**

**A. Summary of Amendments**

We are adopting revisions to the transaction eligibility requirements of Forms S-3 and F-3 that will allow companies to take advantage of these forms for primary offerings regardless of the size of their public float. Whereas secondary offerings may be registered on Forms S-3 and F-3 irrespective of float, the instructions to Forms S-3 and F-3 have, before now, restricted the use of these forms for primary securities offerings to companies that have a minimum of \$75 million in public float calculated within 60 days prior to the date the registration statement is filed. To expand the availability of Forms S-3 and F-3 for primary offerings to more companies, we are adopting revisions to these forms that allow companies with less than \$75 million in public float to

register primary offerings of their securities on Forms S-3 and F-3, provided:

- They meet the other registrant eligibility conditions for the use of Form S-3 or Form F-3, as applicable;
- They have at least one class of common equity securities listed and registered on a national securities exchange;
- They do not sell more than the equivalent of one-third of their public float in primary offerings under General Instruction I.B.6. of Form S-3 or under General Instruction I.B.5. of Form F-3, as applicable, over the previous period of 12 calendar months; and
- They are not shell companies and have not been shell companies for at least 12 calendar months before filing the registration statement.

**B. Benefits**

The ability to conduct primary offerings on Forms S-3 and F-3 confers significant advantages on eligible companies in terms of cost savings and capital formation. The time required to prepare Form S-3 or Form F-3 is significantly lower than that required for Forms S-1 and F-1.<sup>112</sup> This difference is magnified by the fact that Form S-3 and Form F-3, unlike Forms S-1 and F-1, permit registrants to forward incorporate required information by reference to disclosure in their Exchange Act filings. Therefore, Form S-3 and Form F-3 registration statements can be automatically updated. This allows such companies to avoid additional delays and interruptions in the offering process and can reduce the costs associated with preparing and filing post-effective

<sup>107</sup> In the Proposing Release, this increase was 10% for each form but has been raised to 15% in light of the 12-month offering restriction on sales being raised from 20% to one-third of a company's public float. That is, because the ceiling has been raised, eligible companies will be able to conduct somewhat larger and/or more frequent offerings on Form S-3 and F-3.

<sup>108</sup> This number adds a 15% premium to the individual totals for each of the registration forms, as follows: Form S-1 (15% of 57, rounded up, equals 9) and Form F-1 (15% of 3, rounded up, equals 1). The sum of these increases, which is equal to 10, is then added to the total of 60 Forms

S-1 and F-1 filed by the subject companies in 2006 that we believe will be filed on Forms S-3 and F-3 by these companies in future years. The total is an estimated increase of 70 Forms S-3 and F-3 (comprised of 66 additional Forms S-3 and four additional Forms F-3).

<sup>109</sup> For discussions of the relative burden of preparation of registration statements under the Securities Act allocated between issuers internally and their outside advisers, see *Executive Compensation and Related Person Disclosure*, Release No. 33-8732A (Aug. 29, 2006) [71 FR 56225] and Release No. 33-8591.

<sup>110</sup> In connection with other recent rulemakings, we have had discussions with several private law firms to estimate an hourly rate of \$400 as the average cost of outside professionals that assist issuers in preparing disclosures and conducting registered offerings.

<sup>111</sup> This reflects current Office of Management and Budget estimates.

<sup>112</sup> The Office of Management and Budget currently estimates the time required to prepare Form S-3 and Form F-3 as 459 hours and 166 hours, respectively. This is contrasted with current estimates for Form S-1 and F-1 as 1,176 hours and 638 hours, respectively.

amendments to the registration statement.

Overall, we anticipate that the expansion of Form S-3 and Form F-3 eligibility will decrease the aggregate costs of complying with the Commission's rules by allowing companies previously eligible to use only Form S-1 or Form F-1 the use of short-form registration on Form S-3 or Form F-3, as applicable. Using our estimates prepared for purposes of the Paperwork Reduction Act, we estimate that under the amendments the annual decrease in the compliance burden for companies to comply with our collection of information requirements to be approximately 10,375 hours of in-house company personnel time (valued at \$1,816,000<sup>113</sup>) and to be approximately \$12,450,000 for the services of outside professionals.

In addition to the benefits associated with the estimated reduction in the time required to prepare Forms S-3 and F-3 in lieu of Forms S-1 and F-1, and a company's ability to forward incorporate prospectus disclosure by reference, Forms S-3 and F-3 provide substantial flexibility to companies raising money in the capital markets, which ultimately may reduce the cost of capital for such companies and facilitate their access to additional sources of investment. Companies that are eligible to use Form S-3 or Form F-3 for primary offerings are able to conduct delayed and continuous registered offerings under Rule 415 of the Securities Act, which provides considerable flexibility in accessing the public securities markets from time to time in response to changes in the market and other factors. Eligible companies are permitted to register securities prior to planning any offering and, once the registration statement is effective, offer these securities in one or more tranches without waiting for further Commission action. By having more control over the timing of their offerings, these companies can take advantage of desired market conditions, thus allowing them to raise capital on more favorable terms (such as pricing) or to obtain lower interest rates on debt. In addition, they can vary certain terms of the securities being offered upon short notice, enabling them to more efficiently meet the competitive requirements of the public securities markets. We believe that extending shelf registration benefits to more companies, in the manner we have chosen, will facilitate the capital-raising efforts of

smaller public companies who currently have fewer financing options than their larger counterparts.<sup>114</sup> Consequently, we anticipate that the amendments will result in smaller issuers raising more capital through the public markets rather than through exempt offerings conducted in the domestic and offshore markets. Investors in these companies will benefit by such companies' improved access to capital on more favorable terms. In particular, investors in smaller public companies may be less subject to the risk of dilution in the value of their shares if the companies in which they invest are able to meet more of their capital needs in the public markets. By selling into the public markets, these companies may be able to avoid the substantial pricing discounts that private investors often demand to compensate them for the relative illiquidity of the restricted shares they are purchasing.<sup>115</sup>

The public registration of securities also provides additional benefits to investors over alternative forms of capital raising. To the extent that the amendments lead to an increase in the use of registered offerings through the use of Form S-3 and Form F-3 as a source of financing and a resulting decrease in private market alternatives, investors in those offerings will benefit from the additional investor protections associated with public registration.

Notwithstanding our belief regarding the beneficial effects of the amendments, however, any resulting benefits that accrue to companies and their investors as a result of these amendments will depend on future market conditions and circumstances unique to each company.

### C. Costs

As discussed in Section B. above, we do not expect that the amendments to Forms S-3 and F-3 will materially increase companies' overall compliance costs associated with preparing, reviewing and filing these registration statements, although there may be some additional costs incurred by companies to monitor their ongoing compliance with the one-third sales cap imposed by the amendments. At the same time, the amendments could result in certain additional market costs that are difficult to quantify. For example, it has been suggested that there are risks inherent in allowing smaller public companies to take advantage of shelf primary offerings on Forms S-3 and F-3. Because this

would permit such companies to avail themselves of periodic takedowns without further Commission action or prior staff review, concerns have been raised about the increased potential for fraud and market manipulation.<sup>116</sup> Although the Commission would retain the authority to review registration statements before declaring them effective, individual takedowns are not subject to prior staff review. Under the current rules, if issuers are instead using Forms S-1 or F-1, they would be required to file separate registration statements for each new offering, which would be subject to selective staff review before going effective. If these issuers can instead conduct shelf offerings on Form S-3 and Form F-3, there may be some loss of the deterrent effect on the companies' disclosures in connection with each takedown off the shelf because of the lack of prior staff review. In addition, the short time horizon of shelf offerings may also reduce the time that participating underwriters have to apply their independent scrutiny and judgment to an issuer's prospectus disclosure. We have also considered the effect the amendments may have on market demand for the securities of smaller public companies offered on Form S-3 and Form F-3. If there is a perception that smaller public company securities offered through shelf registration statements are more prone to abuse because of the lack of involvement by the Commission staff, this may erode investor confidence in these offerings generally. This could, in turn, make it more difficult for these companies to raise capital and significantly negate some of the benefits of the rule.

While we recognize that extending the benefits of shelf registration to an expanded group of companies will limit the staff's direct involvement in takedowns of securities off the shelf and could therefore pose some risk to investors, we believe that the risks are justified by the benefits that we anticipate will accrue by facilitating the capital formation efforts of smaller public companies. As we have discussed elsewhere in this release, we believe these risks have been mitigated by the emergence of the Internet which, in combination with the Commission's EDGAR database, has greatly enhanced the ability of the market to readily digest and assimilate public company information.

However, in order minimize risks to investors, the amendments include certain restrictions intended to moderate the impact of expanding

<sup>113</sup> Consistent with recent rulemaking releases, we estimate the value of work performed by the company internally at a cost of \$175 per hour.

<sup>114</sup> See generally, Chaplinsky and Haushalter, *Financing Under Extreme Uncertainty: Contract Terms and Returns to Private Investments in Public Equity*.

<sup>115</sup> *Id.*

<sup>116</sup> See n. 34.

Forms S-3 and F-3 eligibility. These are:

- Excluding shell companies from eligibility;
- Requiring that companies have at least one class of common equity securities listed and registered on a national securities exchange; and
- Imposing a cap of one-third of a company's public float on the amount of securities that can be sold into the market in any period of 12 calendar months by eligible issuers on Forms S-3 and F-3.

We note, however, that monitoring compliance with the one-third cap may be difficult given the lack of staff review before a shelf offering.

#### IV. Consideration of Promotion of Efficiency, Competition and Capital Formation

Securities Act Section 2(b)<sup>117</sup> requires us, when engaging in rulemaking where we are required to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.

We expect the amendments will increase efficiency and enhance capital formation by facilitating the ability of smaller public companies to access the capital markets consistent with investor protection. Prior to these amendments, many companies have been ineligible to use Forms S-3 and F-3 to register primary offerings of their securities because the size of their public float did not satisfy the \$75 million threshold required by these forms. Consequently, they have been unable to take advantage of the important benefits enjoyed by eligible companies, the most significant of which is the ability to conduct primary offerings on a delayed and continuous basis. The ability to register securities that may be taken off the shelf as needed, without prior staff review, provides a powerful tool for capital formation because it allows companies the flexibility to take advantage of desired market conditions efficiently and upon short notice. Companies may be able to raise capital more cheaply, quickly, and on more favorable terms than would otherwise be the case. By selling into the public markets, these companies may be able to avoid the substantial pricing discounts that private investors often demand to compensate them, in part, for the relative illiquidity of the restricted shares they are purchasing.<sup>118</sup>

We therefore believe that extending shelf registration benefits to more companies in the manner that we have chosen will facilitate the capital-raising efforts of smaller public companies who currently have fewer financing options than their larger counterparts.<sup>119</sup> Consequently, we anticipate that the amendments will lead to efficiencies in capital formation, as smaller issuers will be able to raise more capital through the public markets rather than through exempt offerings conducted in the domestic and offshore markets.

At the same time, we have also considered the potential that the amendments might result in certain additional market costs that could limit any efficiencies realized. For example, it has been suggested that extending the benefits of shelf registration to an expanded group of companies will limit the staff's direct involvement in takedowns of securities off the shelf and could therefore pose some risk to investors. In addition, the short time horizon of shelf offerings also may reduce the time that participating underwriters have to apply their independent scrutiny and judgment to an issuer's prospectus disclosure. By reducing this staff and underwriter oversight, there is a risk that these securities offerings may be more vulnerable to abuses. Moreover, because companies with a smaller market capitalization, as a group, have a comparatively smaller market following than larger, well-seasoned issuers and are more thinly traded, smaller companies' securities may be more vulnerable to potential manipulative practices. We also have considered the effect the amendments may have on market demand for the securities of smaller public companies offered on Form S-3 and Form F-3. If there is a perception that smaller public company securities offered through shelf registration statements are more prone to abuse because of the lack of prior involvement by the Commission staff, this may erode investor confidence in these offerings generally. This could, in turn, make it more difficult for these companies to raise capital and significantly negate the benefits of the rule.

The effects of the amendments on competition are difficult to predict, but it is possible that making it easier for smaller public issuers to access the domestic public securities markets will lead to a reallocation of capital, as companies that previously had little choice but to offer their securities in private offerings or in offshore markets

because of their Form S-3 and Form F-3 ineligibility will now find it cost-effective to offer their securities domestically in primary offerings on Form S-3 and Form F-3. If such a reallocation occurs, it may also impact securities market professionals, such as finders, brokers and agents, who specialize in facilitating private securities offerings. The demand for these services may shift to the public markets, where other professionals, such as investment banks that underwrite public offerings, have a comparative advantage.

#### V. Final Regulatory Flexibility Act Analysis

This Final Regulatory Flexibility Act Analysis has been prepared in accordance with 5 U.S.C. 603. It relates to revisions to the eligibility requirements for the use of registration statements on Forms S-3 and F-3 to register primary offerings of securities.

##### A. Need for the Amendments

Prior to these amendments, many smaller public companies have been ineligible to use Forms S-3 and F-3 to register primary offerings of their securities because the size of their public float did not satisfy the \$75 million threshold required by these forms. Consequently, they have been unable to take advantage of the important benefits enjoyed by eligible companies, the most significant of which is the ability to conduct primary offerings on a delayed and continuous basis. The ability to register securities that may be taken off the shelf as needed, without prior staff review, provides a powerful tool for capital formation because it allows companies the flexibility to take advantage of desired market conditions efficiently and on short notice. As such, eligible companies may be able to raise capital more cheaply, quickly, and on more favorable terms than would otherwise be the case. Without this source of financing, smaller public companies that are not eligible to register primary offerings on Form S-3 or Form F-3 currently have fewer, and less favorable, financing options than their larger Form S-3 and F-3-eligible counterparts.

##### B. Significant Issues Raised by Public Comment

In the Proposing Release, we requested comment on any aspect of the Initial Regulatory Flexibility Act Analysis, including the number of small entities that would be affected by the proposals, and both the qualitative and quantitative nature of the impact. Several commenters supported the

<sup>117</sup> 15 U.S.C. 77b(b).

<sup>118</sup> See n. 115.

<sup>119</sup> See n. 114.

proposal because they believed it would benefit smaller public companies, but did not provide any specific comments on the Initial Regulatory Flexibility Act Analysis.

### C. Small Entities Subject to the Amendments

The Regulatory Flexibility Act defines “small entity” to mean “small business,” “small organization,” or “small governmental jurisdiction.”<sup>120</sup> The Commission’s rules define “small business” and “small organization” for purposes of the Regulatory Flexibility Act for each of the types of entities regulated by the Commission.<sup>121</sup> Roughly speaking, a “small business” and “small organization,” when used with reference to an issuer other than an investment company, means an issuer with total assets of \$5 million or less on the last day of its most recent fiscal year. We estimate that there are approximately 1,100 issuers, other than investment companies, that may be considered reporting small entities.<sup>122</sup>

The amendments will affect small entities that:

- Are not shell companies;
- Have at least one class of common equity securities listed and registered on a national securities exchange; and
- Satisfy the registrant eligibility requirements for the use of Form S-3 or Form F-3, which generally pertain to a company’s reporting history under the Exchange Act.<sup>123</sup>

Based on these registrant eligibility requirements, we estimate that there are approximately 115 to 350 small entities that will be affected by the amendments and therefore will become eligible to use Form S-3 or Form F-3 for primary securities offerings.<sup>124</sup>

<sup>120</sup> 5 U.S.C. 601(6).

<sup>121</sup> Rules 157 under the Securities Act [17 CFR 230.157], 0-10 under the Exchange Act [17 CFR 240.0-10] and 0-10 under the Investment Company Act [17 CFR 270.0-10] contain the applicable definitions.

<sup>122</sup> The estimated number of reporting small entities is based on 2007 data, including the Commission’s EDGAR database and Thomson Financial’s Worldscope database. See also Revisions to *Rule 144 and Rule 145 to Shorten Holding Period for Affiliates and Non-Affiliates*, Release No. 33-8813 (June 20, 2007) [72 FR 36822, 36841-36842]. This represents an update from the number of reporting small entities estimated in prior rulemakings. See, for example, *Executive Compensation and Related Disclosure*, Release No. 33-8732A (Aug. 29, 2006) [71 FR 53158] (in which the Commission’s estimated a total of 2,500 small entities, other than investment companies).

<sup>123</sup> See n. 37 and n. 83.

<sup>124</sup> The burden estimates for small entities are presented as a range representing the minimum and maximum number of small entities that we estimate would currently qualify for eligibility under either General Instruction I.B.6. of Form S-3 or General Instruction I.B.5. of Form F-3, as applicable, based on data available to us.

### D. Reporting, Recordkeeping and Other Compliance Requirements

Because Forms S-3 and F-3 are abbreviated registration forms that can be updated automatically through incorporation by reference of a registrant’s Exchange Act filings, we believe use of the forms by eligible small entities will decrease their existing compliance burden. Because the amendments have little effect on the information disclosure requirements of Form S-3 or Form F-3,<sup>125</sup> we do not believe that the costs of complying with the amendments for small entities will be disproportionate to that of large entities.<sup>126</sup> We recognize, however, that there will be some additional costs associated with an issuer’s need to continually monitor its compliance with the one-third cap on sales in any period of 12 calendar months, but we believe that any such costs will be insignificant.

For purposes of the Paperwork Reduction Act, we estimate the annual decrease in the paperwork burden for small entities to comply with our collection of information requirements to be approximately between 3,843 and 14,168 hours of in-house company personnel time (valued between \$673,000 to 2,480,000<sup>127</sup>) and to be approximately between \$4,612,000 and \$17,001,000 for the services of outside professionals.

### E. Agency Action to Minimize Effect on Small Entities

The Regulatory Flexibility Act directs us to consider significant alternatives that would accomplish the stated objectives, while minimizing any significant adverse impact on small entities. In connection with the

<sup>125</sup> See n. 96. Instruction 7 to new General Instruction I.B.6. of Form S-3 and Instruction 7 to new General Instruction I.B.5. of Form F-3 require disclosure of the registrant’s updated calculation of public float and the amount of securities offered on Form S-3 or F-3, as applicable, pursuant to this instruction during the prior 12 calendar months, but we believe any burden associated with this requirement will be minimal.

<sup>126</sup> It should be noted, however, that General Instruction I.C. of Form S-3 currently requires:

\* \* \* smaller reporting compan[ies] (as defined in Rule 405 of the Securities Act [17 CFR 230.405]) that [are] eligible to use Form S-3 shall use the disclosure items in Regulation S-K [17 CFR 229.10 *et seq.*] with specific attention to the subparagraph describing scaled disclosure, if any. Smaller reporting companies may provide the financial information called for by Item 310 of Regulation S-K in lieu of the financial information called for by Item 11 in this form.

Release No. 33-8876. Because such scaled disclosure requirements generally allow scaled disclosure for smaller reporting companies, small entities that file on Form S-3 may have a comparatively lesser compliance burden overall than larger issuers.

<sup>127</sup> See n. 113.

amendments, the Regulatory Flexibility Act requires that we consider the following alternatives:

1. Establishing different compliance or reporting requirements which take into account the resources available to smaller entities;
2. The clarification, consolidation or simplification of disclosure for small entities;
3. Use of performance standards rather than design standards; and
4. Exempting smaller entities from coverage of the disclosure requirements, or any part thereof.

Of these alternatives, only the last appears germane to these amendments. Alternative 3 is not applicable, as the distinction between performance standards and design standards has no bearing on the amendments. Alternatives 1 and 2, because they pertain to establishing different or simplified reporting requirements for smaller entities, also would not seem helpful in this instance because our amendments are already expected to reduce the compliance burden on eligible smaller entities. Regarding Alternatives 1, 2 and 4, we considered relaxing the transaction eligibility requirements for Forms S-3 and F-3 to a greater degree than we are adopting, which would have the effect of further reducing the compliance burden among smaller entities by making more entities eligible for short-form disclosure. As we stated, however, we decline at this time to adopt a less restrictive eligibility requirement. We believe at this time that imposing the one-third cap on the amount of securities that smaller public companies listed on exchanges may sell pursuant to primary offerings on Forms S-3 and F-3, as described, will help to facilitate capital formation through the securities markets consistent with our primary objective of investor protection.

## VI. Statutory Authority and Text of the Amendments

The amendments described in this release are being adopted under the authority set forth in Sections 6, 7, 8, 10 and 19(a) of the Securities Act, as amended.

### List of Subjects in 17 CFR Parts 230 and 239

Reporting and recordkeeping requirements, Securities.

■ For the reasons set out in the preamble, the Commission amends title 17, chapter II, of the Code of Federal Regulations as follows:

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

■ 1. The authority citation for part 230 continues to read in part as follows:

**Authority:** 15 U.S.C. 77b, 77c, 77d, 77f, 77g, 77h, 77j, 77r, 77s, 77z-3, 77sss, 78c, 78d, 78j, 78l, 78m, 78n, 78o, 78t, 78w, 78ll(d), 78mm, 80a-8, 80a-24, 80a-28, 80a-29, 80a-30, and 80a-37, unless otherwise noted.

\* \* \* \* \*

■ 2. Amend § 230.401 by:

■ a. in paragraph (g)(1), revising the cite “paragraph (g)(2)” to read “paragraphs (g)(2) and (g)(3)”; and

■ b. adding paragraph (g)(3).

The addition reads as follows:

**§ 230.401 Requirements as to proper form.**

\* \* \* \* \*

(g) \* \* \*

(3) Violations of General Instruction I.B.6. of Form S-3 or General Instruction I.B.5. of Form F-3 will also violate the requirements as to proper form under this section notwithstanding that the registration statement may have been declared effective previously.

**PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933**

■ 3. The authority citation for part 239 continues to read in part as follows:

**Authority:** 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z-2, 77z-3, 77sss, 78c, 78l, 78m, 78n, 78o(d), 78u-5, 78w(a), 78ll, 77mm, 80a-2(a), 80a-3, 80a-8, 80a-9, 80a-10, 80a-13, 80a-24, 80a-26, 80a-29, 80a-30, and 80a-37, unless otherwise noted.

\* \* \* \* \*

■ 4. Amend Form S-3 (referenced in § 239.13) by adding General Instruction I.B.6. to read as follows:

**Note:** The text of Form S-3 does not, and this amendment will not, appear in the Code of Federal Regulations.

**FORM S-3—REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

\* \* \* \* \*

**General Instructions**

**I. Eligibility Requirements for Use of Form S-3 \* \* \***

*B. Transaction Requirements. \* \* \**

6. *Limited Primary Offerings by Certain Other Registrants.* Securities to be offered for cash by or on behalf of a registrant; *provided that:*

(a) the aggregate market value of securities sold by or on behalf of the registrant pursuant to this Instruction I.B.6. during the period of 12 calendar months immediately prior to, and including, the sale is no more than one-

third of the aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant;

(b) the registrant is not a shell company (as defined in § 230.405 of this chapter) and has not been a shell company for at least 12 calendar months previously and if it has been a shell company at any time previously, has filed current Form 10 information with the Commission at least 12 calendar months previously reflecting its status as an entity that is not a shell company; and

(c) the registrant has at least one class of common equity securities listed and registered on a national securities exchange.

*Instructions.*

1. “Common equity” is as defined in Securities Act Rule 405 (§ 230.405 of this chapter). For purposes of computing the aggregate market value of the registrant’s outstanding voting and non-voting common equity pursuant to General Instruction I.B.6., registrants shall use the price at which the common equity was last sold, or the average of the bid and asked prices of such common equity, in the principal market for such common equity as of a date within 60 days prior to the date of sale. See the definition of “affiliate” in Securities Act Rule 405 (§ 230.405 of this chapter).

2. For purposes of computing the aggregate market value of all securities sold by or on behalf of the registrant in offerings pursuant to General Instruction I.B.6. during any period of 12 calendar months, registrants shall aggregate the gross proceeds of such sales; *provided*, that, in the case of derivative securities convertible into or exercisable for shares of the registrant’s common equity, registrants shall calculate the aggregate market value of any underlying equity shares in lieu of the market value of the derivative securities. The aggregate market value of the underlying equity shall be calculated by multiplying the maximum number of common equity shares into which the derivative securities are convertible or for which they are exercisable as of a date within 60 days prior to the date of sale, by the same per share market price of the registrant’s equity used for purposes of calculating the aggregate market value of the registrant’s outstanding voting and non-voting common equity pursuant to Instruction 1 to General Instruction I.B.6. If the derivative securities have been converted or exercised, the aggregate market value of the underlying equity shall be calculated by multiplying the actual number of shares

into which the securities were converted or received upon exercise, by the market price of such shares on the date of conversion or exercise.

3. If the aggregate market value of the registrant’s outstanding voting and non-voting common equity computed pursuant to General Instruction I.B.6. equals or exceeds \$75 million subsequent to the effective date of this registration statement, then the one-third limitation on sales specified in General Instruction I.B.6(a) shall not apply to additional sales made pursuant to this registration statement on or subsequent to such date and instead the registration statement shall be considered filed pursuant to General Instruction I.B.1.

4. The term “Form 10 information” means the information that is required by Form 10 or Form 20-F (§ 249.210 or § 249.220f of this chapter), as applicable to the registrant, to register under the Securities Exchange Act of 1934 each class of securities being registered using this form. A registrant may provide the Form 10 information in another Commission filing with respect to the registrant.

5. The date used in Instruction 2 to General Instruction I.B.6. shall be the same date used in Instruction 1 to General Instruction I.B.6.

6. A registrant’s eligibility to register a primary offering on Form S-3 pursuant to General Instruction I.B.6. does not mean that the registrant meets the requirements of Form S-3 for purposes of any other rule or regulation of the Commission apart from Rule 415(a)(1)(x) (§ 230.415(a)(1)(x) of this chapter).

7. Registrants must set forth on the outside front cover of the prospectus the calculation of the aggregate market value of the registrant’s outstanding voting and non-voting common equity pursuant to General Instruction I.B.6. and the amount of all securities offered pursuant to General Instruction I.B.6. during the prior 12 calendar month period that ends on, and includes, the date of the prospectus.

8. For purposes of General Instruction I.B.6(c), a “national securities exchange” shall mean an exchange registered as such under Section 6(a) of the Securities Exchange Act of 1934.

\* \* \* \* \*

■ 5. Amend Form F-3 (referenced in § 239.33) by adding General Instruction I.B.5. to read as follows:

**Note:** The text of Form F-3 does not, and this amendment will not, appear in the Code of Federal Regulations.

**FORM F-3—REGISTRATION  
STATEMENT UNDER THE  
SECURITIES ACT OF 1933**

\* \* \* \* \*

**General Instructions**

**I. Eligibility Requirements for Use of  
Form F-3 \* \* \***

*B. Transaction Requirements \* \* \**

5. *Limited Primary Offerings by Certain Other Registrants.* Securities to be offered for cash by or on behalf of a registrant; *provided that:*

(a) the aggregate market value of securities sold by or on behalf of the registrant pursuant to this Instruction I.B.5. during the period of 12 calendar months immediately prior to, and including, the sale is no more than one-third of the aggregate market value worldwide of the voting and non-voting common equity held by non-affiliates of the registrant;

(b) the registrant is not a shell company (as defined in § 230.405 of this chapter) and has not been a shell company for at least 12 calendar months previously and if it has been a shell company at any time previously, has filed current Form 10 information with the Commission at least 12 calendar months previously reflecting its status as an entity that is not a shell company; and

(c) the registrant has at least one class of common equity securities listed and registered on a national securities exchange.

*Instructions.*

1. “Common equity” is as defined in Securities Act Rule 405 (§ 230.405 of this chapter). For purposes of computing the aggregate market value of the registrant’s outstanding voting and non-voting common equity pursuant to General Instruction I.B.5., registrants shall use the price at which the common equity was last sold, or the average of the bid and asked prices of such common equity, in the principal market for such common equity as of a date

within 60 days prior to the date of sale. See the definition of “affiliate” in Securities Act Rule 405 (§ 230.405 of this chapter).

2. For purposes of computing the aggregate market value of all securities sold by or on behalf of the registrant in offerings pursuant to General Instruction I.B.5. during any period of 12 calendar months, registrants shall aggregate the gross proceeds of such sales; *provided*, that, in the case of derivative securities convertible into or exercisable for shares of the registrant’s common equity, registrants shall calculate the aggregate market value of any underlying equity shares in lieu of the market value of the derivative securities. The aggregate market value of the underlying equity shall be calculated by multiplying the maximum number of common equity shares into which the derivative securities are convertible or for which they are exercisable as of a date within 60 days prior to the date of sale, by the same per share market price of the registrant’s equity used for purposes of calculating the aggregate market value of the registrant’s outstanding voting and non-voting common equity pursuant to Instruction 1 to General Instruction I.B.5. If the derivative securities have been converted or exercised, the aggregate market value of the underlying equity shall be calculated by multiplying the actual number of shares into which the securities were converted or received upon exercise, by the market price of such shares on the date of conversion or exercise.

3. If the aggregate market value of the registrant’s outstanding voting and non-voting common equity computed pursuant to General Instruction I.B.5. equals or exceeds \$75 million subsequent to the effective date of this registration statement, then the one-third limitation on sales specified in General Instruction I.B.5(a) shall not apply to additional sales made pursuant to this registration statement on or

subsequent to such date and instead the registration statement shall be considered filed pursuant to General Instruction I.B.1.

4. The term “Form 10 information” means the information that is required by Form 10 or Form 20-F (§ 249.210 or § 249.220f of this chapter), as applicable to the registrant, to register under the Securities Exchange Act of 1934 each class of securities being registered using this form. A registrant may provide the Form 10 information in another Commission filing with respect to the registrant.

5. The date used in Instruction 2 to General Instruction I.B.5. shall be the same date used in Instruction 1 to General Instruction I.B.5.

6. A registrant’s eligibility to register a primary offering on Form F-3 pursuant to General Instruction I.B.5. does not mean that the registrant meets the requirements of Form F-3 for purposes of any other rule or regulation of the Commission apart from Rule 415(a)(1)(x) (§ 230.415(a)(1)(x) of this chapter).

7. Registrants must set forth on the outside front cover of the prospectus the calculation of the aggregate market value of the registrant’s outstanding voting and non-voting common equity pursuant to General Instruction I.B.5. and the amount of all securities offered pursuant to General Instruction I.B.5. during the prior 12 calendar month period that ends on, and includes, the date of the prospectus.

8. For purposes of General Instruction I.B.5(c), a “national securities exchange” shall mean an exchange registered as such under Section 6(a) of the Securities Exchange Act of 1934.

\* \* \* \* \*

By the Commission.

Dated: December 19, 2007.

**Nancy M. Morris,**  
*Secretary.*

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