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Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, D.C. 20549-0609

Securities Offering Reform
Commission File No. S7-38-04

Dear Mr. Katz:

We are pleased to comment on the proposal by the Securities and Exchange Commission (the Commission or the SEC) that would streamline the registration, communications, and offering processes under the Securities Act of 1933 (the Act). Overall, we support the proposal and agree with the Commission's approach in making fundamental, but incremental, improvements to the existing integrated disclosure and shelf registration systems. We believe that the proposal would eliminate unnecessary obstacles to capital formation while preserving the quality of financial reporting. However, we are particularly concerned that the proposal would not require an auditor's consent in connection with a prospectus supplement that would create a new effective date for the related registration statement. In addition, we suggest that the SEC consider making additional reforms. Our comments and recommendations regarding the proposal are discussed in detail below.

General

We support those aspects of the Commission's proposal that would allow issuers more freedom to communicate information and that would allow larger issuers to control the timing of their registered securities offerings. We believe that the proposed changes would improve the public offering process, specifically those:

- Providing automatic shelf registration for offerings by certain larger issuers, with pay-as-you-go registration fees;
- Permitting immediate takedowns from shelf registration statements by seasoned issuers;
- Eliminating the limitation that issuers only register securities they intend to offer within two years by requiring the issuer to update its shelf registration statement at least every three years;

- Liberalizing the permitted communications around the time of a registered securities offering; and
- Establishing that prospectus access equals prospectus delivery.

Auditor Association with Prospectus Supplements

As proposed, a prospectus supplement relating to a takedown of securities off of a shelf registration would (a) be considered to be part of the registration statement for Section 11 liability purposes, and (b) establish a new effective date, for liability purposes only, for the shelf registration statement. The proposed rule states that the new effective date in those circumstances would be for liability purposes only and would not, by itself, require the filing of additional consents of experts.

If the SEC adopts the proposal such that a prospectus supplement establishes a new effective date for the shelf registration statement for purposes of Section 11 liability, we would object if the filing of a prospectus supplement did not also require an updated consent of named experts. We are concerned that, without a formal consent requirement, independent public accounting firms, whether or not registered with the PCAOB, would not always be able to comply with the respective auditing standards of the PCAOB and AICPA. Those standards require the auditor to perform post-report review procedures up to the effective date or as close thereto as is reasonable and practicable in the circumstances. These procedures also provide important investor protections.

Section 11 of the Act provides for liability if any part of a registration statement contains material omissions or misstatements. Section 11 liability applies not only to underwriters, directors, and those who sign the registration statement on behalf of the issuer, but also to named experts, such as the issuer's independent registered public accounting firm and any auditors of other financial statements that may be required in the registration statement (e.g., significant acquired businesses, significant equity investees). Specifically, Section 11(a) of the Act provides that such persons may be sued by anyone acquiring that security if any part of the registration statement contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading. Given the scope and basis of Section 11 liability, it is not clear to us how a prospectus supplement could be considered to create a new effective date "for liability purposes only" without also requiring the issuer and others with Section 11 liability to consider the adequacy and accuracy of disclosures in the registration statement (including the prospectus supplement) as of the new effective date.

Section 11(b)(3) of the Act provides that a named expert would not be liable if he sustains the burden of proof that he had, after reasonable investigation, reasonable ground to believe and did believe, at the time the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading. Section 11(c) of the Act provides that the standard of reasonableness for purposes of determining what constitutes a reasonable investigation and a reasonable ground for belief under Section 11(b)(3) "…shall be that required of a prudent man in the management of his own property." Such reasonable investigation is commonly referred to as a "due diligence" defense.

AU 711, *Filings Under Federal Securities Statutes*, requires the auditor to perform certain procedures in connection with an offering of securities under the Act. The purpose of the auditor performing these procedures is to become aware of any events that may require adjustment to or disclosure in the financial statements. In addition, these procedures sustain the burden of proof that the auditor has made a "reasonable investigation" under Section 11(b)(3) of the Act (i.e., the procedures represent the auditor's due diligence). The procedures clearly require the auditor to anticipate the effective date of the registration statement and to commence the procedures sufficiently in advance of that date to assure their timely completion.

At or near the effective date, AU 711 requires the auditor to perform procedures, as specified in AU 560.12, with respect to subsequent events that may require adjustment to or disclosure in the financial statements in order for them to be fairly stated in conformity with generally accepted accounting principles. Such subsequent events procedures should include:

- Reading the latest available interim financial statements and comparing them with the audited financial statements;
- Inquiring of officers and other executives having responsibility for financial and accounting matters whether the interim statements have been prepared on the same basis as that used for the audited financial statements;
- Inquiring of, and discussing with, such officers and other executives as to (a) substantial contingent liabilities or commitments at the date of the audited balance sheet and arising subsequently, (b) any significant change in the capital stock, long-term debt, or working capital, (c) the current status of items that were accounted for in the audited financial statements on the basis of tentative, preliminary, or inconclusive data, and (d) any unusual adjustments subsequent to the date of the audited balance sheet;
- Reading available minutes of meetings of stockholders, directors, and appropriate committees; as to meetings for which minutes are not available, inquiring about matters dealt with at such meetings;
- Inquiring of company's legal counsel concerning litigation, claims, and assessments; and
- Obtaining a letter of representations from appropriate officials (e.g., CEO and CFO) as to whether any events occurred subsequent to the date of the audited financial statements that in the officer's opinion would require adjustment to or disclosure in these statements.

In addition, AU 711.10 requires the auditor to perform the following additional procedures, at or near the effective date:

- Reading the entire prospectus and other pertinent portions of the registration statement; and
- Inquiring of, and obtaining written representations from, officers and other executives responsible for financial and accounting matters about whether any events have occurred, other than those reflected or disclosed in the registration statement, that, in the officers' or other executives' opinion, would have a material effect on the audited financial statements included therein or that should be disclosed in order to keep those statements from being misleading.

Section 7(a) of the Act states (in part), "If … any person whose profession gives authority to a statement made by him, is named as having prepared or certified any part of the registration statement, or is named as having prepared or certified a report or valuation for use in connection with the registration statement, the written consent of such person shall be filed with the registration statement." Historically, the SEC staff has required auditors to update their consent whenever a company files a post-effective amendment or an annual report that creates a new effective date. The primary purpose of obtaining a written updated consent is to assure that the auditor is aware of the use of its report and the context in which that report is used. Unless the auditor has completed the procedures specified by AU 711, and resolved any concerns identified as a result of those procedures, the auditor would not be able to provide its consent.

At the effective date of any registration statement, we believe that there should be an explicit requirement for a currently dated, signed consent from any auditor whose report is part of that registration statement. In our view, such consent requirement should apply equally at the initial effective date of the registration statement, upon any post-effective amendment, upon the filing of the issuer's annual report that creates a new effective date, and, if adopted, upon the filing of any prospectus supplement that creates a new effective date. The requirement for such a consent from the auditor would continue to confirm that the auditor has had the opportunity to perform the post-report review procedures required by the relevant auditing standards. Consents also enable auditors to fulfill their traditional gatekeeper role regarding registered securities offerings. We do not think that requiring an auditor's consent upon the filing of a prospectus supplement would adversely delay capital formation, provided that the issuer gives adequate notice to the auditor and cooperates as necessary for the auditor to comply with AU 711. However, to the extent that the filing of a prospectus supplement is delayed because the issuer had to address comments and concerns raised by its auditor, any such delay would be in the interest of investor protection.

We would expect that others subject to Section 11 liability would share our concern about having sufficient opportunity to perform their own "reasonable investigation" under Section 11(b)(3) of the Act prior to the filing date of any prospectus supplement that creates a new effective date for the registration statement. Accordingly, the SEC should consider requiring an issuer to obtain, in advance of the filing date, the signed acknowledgment of such persons that they are aware of the issuer's proposed filing.

Well-Known Seasoned Issuers

The Commission's proposal would define a new class of issuers called "well-known seasoned issuers." As proposed, well-known seasoned issuers would be permitted automatic shelf registration for filings on Forms S-3 or F-3, under which shelf registration statements, post effective amendments, and prospectus supplements would become effective upon filing and would not be subject to SEC staff review. We concur with the Commission that automatic shelf registration should be limited to those issuers that satisfy the objectives of the proposed definition of a "well-known seasoned issuer" and that are not otherwise "ineligible" issuers. However, we have specific comments about the proposed definition of a well-known seasoned issuer. In addition, we have further comments below about the proposed definition of an ineligible issuer.

Definition of a Well-Known Seasoned Issuer

We concur with the Commission that well-known seasoned issuer status should be limited to those issuers that "have a reporting history under the Exchange Act and are presumptively the most widely followed in the marketplace."

As proposed, a "well-known seasoned issuer" would be a timely reporting issuer (i.e., one that has timely filed all required Exchange Act reports during the past 12 months), that has either (a) public common equity float of $700 million or more; or (b) for purposes of registering only debt securities, at least $1 billion aggregate amount of registered debt securities issued in the last 3 years. The proposed definition would require an issuer to determine its eligibility as a well-known seasoned issuer as of the last business day of the second fiscal quarter of the most recent fiscal year for which it has filed its SEC annual report on Form 10-K or Form 20-F. This measurement date would be consistent with the determination of the amount of public common equity float disclosed on the cover page of Form 10-K, which currently is used in determining whether an issuer is an accelerated filer.

<u>Size Criteria:</u> In order to ensure that well-known seasoned issuer status would be available only to the most widely followed issuers that have a well-established reporting history under the Exchange Act, the Commission should consider other size tests in addition to public common equity float and volume of recently-issued registered debt. For example, experience during the Internet bubble suggests that smaller issuers with a limited operating history may develop a significant public float based on what an exuberant market perceives to be a promising business plan. Yet, these issuers may not be widely followed and may not have well-established or

sustainable operations. We think that annual revenue (or total assets in the case of a financial institution) might be an appropriate additional measure to assure that a company has substantive operations and resources before it qualifies as a well-known seasoned issuer. We would encourage the SEC's Office of Economic Analysis to conduct further research to evaluate the effects of such an additional test and to determine the appropriate dollar threshold of annual revenue (or total assets in the case of a financial institution) for well-known seasoned issuer eligibility.

In addition, we suggest that the determination of public common equity float and volume of recently-issued registered debt for purposes of qualifying as a well-known seasoned issuer be made as of a date within 60 days of the date the registration statement is filed. This approach would be more consistent with the requirements in Form S-3 for purposes of determining whether a registrant has sufficient public common equity float to be eligible to use Form S-3. We see no need for the determination of well-known seasoned issuer status to be made as of the same date that the determination of accelerated filer status is made. For purposes of determining accelerated filer status, the Commission selected the end of the most recently completed second fiscal quarter in order to provide companies and their auditors needed time to plan for the reporting deadline applicable to that year-end. This same concern is not present for the determination of well-known seasoned issuer status and, therefore, a measurement date closer to the filing date of the shelf registration statement, post effective amendment, or prospectus supplement would be more appropriate in determining that the issuer is of sufficient size as of those dates.

Reporting History Criterion: As proposed, an issuer would qualify as a well-known seasoned issuer if, among other things, it had been subject to the reporting requirements of the Exchange Act for at least twelve months, similarly determined as of the last business day of the second fiscal quarter of the most recent fiscal year for which it has filed its SEC annual report on Form 10-K or Form 20-F. We are concerned that the proposed definition would not ensure that an issuer has a well-established history of meeting its public disclosure obligations. In our view, for purposes of qualifying as a well-known seasoned issuer, an issuer should have a longer history of financial reporting under the Exchange Act (e.g., at least three years). A minimum reporting history of three years would ensure that the SEC staff has conducted at least one review of the issuer's Exchange Act report pursuant to Section 408 of the Sarbanes-Oxley Act of 2002, following the review of its initial registration statement.

Definition of an Accelerated Filer

In our comment letter on Release No. 33-8477, *Temporary Postponement of the Final Phase-In Period for Acceleration of Periodic Report Filing Dates*, we agreed that the Commission should postpone the scheduled final phase-in of the accelerated filing deadlines. We also recommended that the Commission continue to monitor and assess the implications, and potential adverse consequences, of shorter filing deadlines and the scope of the definition of accelerated filers. Specifically, we suggested that the Commission consider the potential adverse effects of accelerated reporting deadlines on the quality control processes of management, the audit committee, and independent registered public accounting firms. Following the current year-end reporting season, we still recommend that the Commission reassess the scheduled acceleration of reporting deadlines, which it has only temporarily postponed.

In our comment letter to Release No. 33-8089, *Acceleration of Periodic Report Filing Dates and Disclosure Concerning Website Access to Reports*, we remarked that the proposed $75 million threshold of public common equity float for purposes of the definition of an accelerated filer, which the SEC ultimately adopted, was too low, which we still believe to be the case. As a result, in our view, many issuers subject to the accelerated reporting deadlines do not have a sufficient market following to warrant the incremental costs of accelerated filing. In light of the Commission's proposed definition of a well-known seasoned issuer, and the analysis underlying the proposed threshold of $700 million in public common equity float, we urge the Commission to raise the current $75 million threshold in the Exchange Act Rule 12b-2 definition of an accelerated filer. In the proposing release, the Commission states, "the issuers that would meet our proposed thresholds for well-known seasoned issuers are thus the most active issuers in the U.S. public capital markets." We believe that well-known seasoned issuers would have the level of market capitalization and investor interest, as well as the available resources, to merit accelerated reporting. Accordingly, the level of public float used to determine well-known seasoned issuer status also should be used to determine accelerated filer status.

Under Rule 12b-2, an issuer remains an accelerated filer until it becomes eligible to file as a small business issuer. In raising the threshold for public common equity float, we recommend that the Commission also reassess the criteria for exiting the accelerated filing deadlines. While we acknowledge the benefits to the market of consistency and predictability in the timing of annual and quarterly reporting by issuers, an issuer should not continue to be subject to shorter reporting deadlines long after it ceases to have a wide market following.

As proposed, certain well-known seasoned issuers (e.g., a debt-only issuer or a majority-owned subsidiary issuer with debt that is fully and unconditionally guaranteed by its parent that is a well-known seasoned issuer) would not meet the definition of an accelerated filer in Rule 12b-2, whether currently or as we have proposed that it be amended. If such issuers avail themselves to the proposed benefits of automatic shelf registration, they also should be required to comply with the accelerated filing deadlines for periodic Exchange Act reports. Otherwise, we concur that such issuers should remain subject to the current 90-day and 45-day deadlines for annual and quarterly reports, respectively. This “opt-in” approach to automatic shelf registration and accelerated reporting would ensure a level playing field among issuers that obtain unfettered access to the public capital markets.

Foreign Private Issuer Considerations

As proposed, the definition of a well-known seasoned issuer applies equally to both domestic issuers and foreign private issuers. While both domestic issuers and foreign private issuers may be widely followed, the extent and timing of information required to be filed by foreign private issuers is significantly less than that of domestic issuers. The integrated disclosure system provides certain accommodations to foreign private issuers including (a) having six months after year-end to file the annual report on Form 20-F, (b) interim reporting on the basis of home country and stock exchange practice rather than quarterly reports, and (c) not being subject to the current reporting requirements of Form 8-K. Thus, a foreign private issuer that meets the proposed definition of a well-known seasoned issuer would receive automatic effectiveness of a shelf registration statement on Form F-3 with financial information that is less timely and less comprehensive than would be required in the Form S-3 of a domestic issuer.

We believe that in order to qualify for automatic effectiveness of a registration statement as a well-known seasoned issuer, the extent and timing of information available to investors at the time of a securities offering should be the same for both domestic issuers and foreign private issuers. Therefore, if foreign private issuers want to avail themselves of the proposed benefits of automatic shelf registration, they should be required to comply with the more rigorous reporting obligations to which domestic issuers adhere. We suggest that the definition of a well-known seasoned issuer should be limited to those foreign private issuers that elect to comply with the domestic reporting forms (i.e., Form 10-K, Form 10-Q, and Form 8-K), subject as well to the accelerated filing deadlines. In addition, we suggest that the Commission consider whether a foreign private issuer should be required to prepare its financial statements on the basis of U.S. GAAP or IFRS in order to qualify as a well-known seasoned issuer.

Ineligible Issuers

We concur with the Commission’s proposal that certain issuers should not be eligible for automatic shelf registration or for the use of the offering communications safe harbors, exemptions, and exclusions. Except as noted below, we concur with the proposed definition of an ineligible issuer. We also agree with the proposed provision that would allow the SEC, for good cause, to determine an issuer (except for a registered investment company or business development company) to be eligible that would otherwise be ineligible.

Going Concern Opinion

As proposed, an issuer would be ineligible if its independent registered public accounting firm modified its report with respect to the latest fiscal year to express substantial doubt about the issuer's ability to continue as a going concern. In our comment letter on Release No. 33-7606A, *The Regulation of Securities Offerings*, we stated our belief that a proposed disqualification as a result of an issuer receiving an auditors' report that contains a going concern explanatory paragraph for the most recent fiscal year would not have any effect on auditors' judgments about the appropriateness of a going concern opinion. While that view has not changed, we question whether the proposed criterion is needed, and we suggest that the SEC either remove or modify it.

In general, we believe that other existing and proposed conditions should be sufficient to address the potential concerns about offerings by issuers with significant liquidity or solvency issues. We observe that one condition to the use of Form S-3 by a seasoned issuer is that, since the fiscal year end reported in its latest SEC annual report, it must not have failed to pay a dividend or sinking fund installment on preferred stock, nor have defaulted on a payment for indebtedness or a long-term lease, which default is material to its consolidated financial position. In addition, as we suggest above, if the public common equity float for purposes of determining eligibility as a well-known seasoned issuer were measured as of a date within 60 days of the filing, a decline in an issuer's equity valuation as a result of its financial distress would make it ineligible for automatic effectiveness, among other things. Further, given the expanded reporting requirements of Form 8-K, particularly Item 2.03, *Creation of a Direct Financial Obligation or an Obligation Under an Off-Balance Sheet Arrangement of a Registrant*, and Item 2.04, *Triggering Events That Accelerate or Increase a Direct Financial Obligation or an Obligation Under an Off-Balance Sheet Arrangement,* we expect that any material deterioration in an issuer's financial condition would become known and be reflected in its credit rating and the market price of its securities.

However, if the SEC concludes that matters involving an issuer's liquidity or solvency should make it an ineligible issuer, we suggest that the related criteria be objectively determinable at the time of an offering. That is, the related criteria should be sensitive to any deterioration in an issuer's financial condition since its fiscal year end, as well as any amelioration of the conditions that led its auditor to issue a going concern opinion with respect to the latest fiscal year.

Material Weaknesses

Although not proposed, the SEC has requested comment on whether a material weakness in internal control over financial reporting should cause an issuer to be an ineligible issuer. We do not believe that a material weakness in internal control over financial reporting should cause an issuer to become ineligible. Until there is more experience with Section 404 reporting and the related incidence and ramifications of material weaknesses, the Commission should not condition the availability of the proposed automatic shelf registration and offering communications safe harbors, exemptions, and exclusions on the absence of any material weaknesses as of an issuer's fiscal year end.

However, if the SEC concludes that a material weakness should make an issuer ineligible, we suggest that the condition of ineligibility be an unremediated material weakness at the time of an offering. That is, the related criterion should be sensitive to a material weakness identified since the issuer's fiscal year end as part of its quarterly evaluation of the effectiveness of disclosure controls and procedures and any material changes in internal control over financial reporting. The related criterion also should not cause an issuer to be ineligible if it has satisfactorily remediated the material weakness that existed at the end of its fiscal year or any subsequent interim fiscal period.

Material Unresolved SEC Staff Comments

We disagree with the Commission's proposal to require disclosure, in the Form 10-K or 20-F of an accelerated filer, of the substance of any material written SEC staff comments made in connection with the review of its Exchange Act reports, if those comments were issued more than 180 days before the end of that fiscal year and remain unresolved at the filing date of the Form 10-K or 20-F.

In the proposing release, the Commission expresses its concern that the proposed automatic effectiveness of registration statements could remove the incentive for well-known seasoned issuers to resolve SEC staff comments in a timely manner. Well-capitalized seasoned issuers generally seek resolution of SEC staff comments on their Exchange Act reports in a timely manner, and we would expect them to continue to do so even if the SEC adopts the proposal. In our experience, SEC staff comments receive a high level of attention, and developing and reviewing responses to the SEC staff often involve the issuer's (a) executive officers, (b) disclosure committee, (c) audit committee, (d) internal and external legal counsel, and (e) independent registered public accounting firm. Also, the quarterly CEO and CFO certifications required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002 have provided added incentive for the timely resolution of SEC staff comments. Further, Section 11 liability for material omissions or misstatements in a registration statement also provides a significant incentive to resolve SEC staff comments prior to the effective date of a new registration statement or the filing date of the Form 10-K or 20-F, which is automatically incorporated by reference into any outstanding shelf registration statement and causes such registration statement to be deemed a new registration statement.

In light of Section 11 liability, particularly with any automatic effectiveness of the registration statements of well-known seasoned issuers, we recommend that the SEC staff implement a protocol to notify an issuer upon the commencement of a review of its Exchange Act reports that could lead to issuance of written comments and the expected timing for receipt of such comments. Such a notification protocol is needed so that a well-known seasoned issuer may reconsider its anticipated timing of a new registration statement, which would become effective immediately, or a prospectus supplement, which, as proposed, would create a new effective date for the related registration statement. We do not think that it is in the best interests of any participants in a securities offering to be unaware that the issuer might soon receive material written comments from the SEC staff.

In addition, we recommend that the SEC staff implement other procedural changes in its reviews of Exchange Act reports, which typically focus on the most recent Form 10-K and any subsequent reports. First, we recommend that, in the normal course, any initial SEC staff comment letter should be issued no later than the end of an issuer's third fiscal quarter. As a result, the SEC staff would have at least six months after the filing of the Form 10-K within which to perform the review and issue any comments. In addition, the issuer would have at least three months within which to resolve the SEC staff's comments prior to its financial statement closing process for the current fiscal year. Second, we recommend that the SEC staff adopt and monitor an administrative policy regarding the timeframes within which the staff will address an issuer's written responses to its comments on Exchange Act Reports, which would supplement its current policy with respect to SEC staff reviews of Securities Act filings. This would encourage the SEC staff to give its reviews of periodic reports and registration statements equal consideration and focus. Accordingly, we recommend that the SEC staff endeavor to either clear or respond to an issuer's written responses within the greater of five working days or the number of days taken by the issuer to respond to the SEC staff's comments on its Exchange Act reports. Such a policy would be a more reasonable and practical way to promote timely resolution of SEC staff comments.

In egregious cases, which we would expect to be rare, if the SEC staff concludes that a well-known seasoned issuer has not adequately addressed a material SEC staff comment, the Commission could always use its authority under Section 8 of the Act and issue a stop order suspending the effectiveness of any registration statement filed by that well-known seasoned issuer.

Given the foregoing, we do not believe that there is any need for disclosure in Exchange Act reports regarding unresolved SEC staff comments. However, should the Commission proceed as proposed, unless the SEC amends the definition of an accelerated filer as we suggest above, the Form 10-K disclosure of material unresolved SEC staff comments should apply only to well-known seasoned issuers, rather than the broader population of accelerated filers as the SEC has proposed. In our view, any additional disclosure should be limited to the group of issuers with which the SEC has concerns regarding reduced incentives for timely comment resolution.

Risk Factors

In our comment letter on Release No. 33-7606A, *The Regulation of Securities Offerings*, we stated our view that risk factor disclosures should be required in Form 10 registration statements and annual reports on Form 10-K, with quarterly updates in Form 10-Q, provided that there also are appropriate private sector or regulatory initiatives to elicit more meaningful risk factor disclosures while eliminating boilerplate. We continue to support the Commission's proposal to require risk factor disclosures in these filings.

Needed Interpretive Guidance

As proposed, registrants would be required to disclose, in plain English, risk factors pursuant to Item 503(c) of Regulation S-K, "including the most significant factors with respect to the registrant's business, operations, industry, or financial position that may have a negative impact on the registrant's future financial performance." Item 503(c) specifies that issuers should describe the "most significant factors that make the offering speculative or risky" but "not present risks that could apply to any issuer." Item 503(c) only specifies that risk factors might include lack of an operating history; lack of recent profitable operations; financial position; business or proposed business; and absence of a market for the issuer's securities.

We remain concerned that without additional interpretive guidance, the quality of risk factor disclosures in Exchange Act reports could vary significantly and become boilerplate. With the increasing focus on enterprise risk management, it would appear that additional guidance could be developed to provide a better framework for identifying and discussing appropriate risk factors. In addition, it would appear that there could be substantial overlap between the proposed disclosure of risk factors and the disclosures of certain uncertainties and risks under Item 303, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, and Item 305, *Quantitative and Qualitative Disclosures about Market Risk*. We also suggest that the Commission provide additional implementation guidance to address its expectations of the extent to which risk factors cited in proposed Item 1A also must be disclosed in MD&A and whether cross referencing would be appropriate to avoid redundancy.

Statutory Safe Harbor

The SEC should extend the statutory safe harbor for forward-looking information (Section 21E of the Exchange Act) to forward-looking statements made pursuant to proposed Item 1A. In FR-67, *Disclosure in Management's Discussion and Analysis about Off-Balance Sheet Arrangements and Aggregate Contractual Obligations*, the Commission stated, "To encourage the type of information and analysis necessary for investors to understand the impact of off-balance sheet arrangements…the amendments include a safe harbor for forward looking information." In that case, the Commission also adopted a provision that the "meaningful cautionary statements" element of the statutory safe harbor would be satisfied if the issuer satisfied all of its off balance sheet disclosure requirements. Because disclosures about risk factors are inherently forward-looking information, we suggest that the SEC extend the statutory safe harbor (including the "meaningful cautionary statements" relief) to forward-looking statements made pursuant to Item 503(c). This would encourage issuers to provide more meaningful disclosure about their risk factors and the potential consequences.

Integrated Reporting

We note that the Commission has not proposed that risk factor disclosures be included in the annual report that must be provided to securities holders under Rule 14a-3(b) of its proxy rules. Given that such an annual report must include the disclosures required by Items 303 and 305 of Regulation S-K, we suggest that the SEC also consider requiring risk factor disclosures in the annual report to securities holders under its proxy rules.

Small Business Issuers

We concur that, as proposed, risk factor disclosures in Exchange Act reports should not extend to small business issuers. Small business issuers are inherently riskier and their most significant risk factors (e.g., lack of financial resources, competition from larger better capitalized companies) usually are clearly evident, and should be sufficiently disclosed, in their MD&A and financial statements. Accordingly, we concur that the proposed risk factor disclosures should not extend to small business issuers, consistent with rationale behind the streamlined disclosure regime the SEC adopted for smaller public companies.

Forward-Looking Information in Initial Public Offerings

The SEC has proposed a safe harbor for reporting issuers that would permit the ongoing communication of regularly released forward-looking information at any time during the offering process. We concur that it would be inappropriate to extend the proposed safe harbor to forward-looking information disclosed by non-reporting issuers outside of the statutory prospectus. However, we encourage the SEC to reassess the scope of the statutory safe harbor for forward-looking statements (Section 27A of the Securities Act).

We recommend that the SEC use its exemptive authority to extend the statutory safe harbor to certain forward-looking statements that are required by SEC regulations in the registration statement of an initial public offering (IPO) by a non-reporting issuer. For example, in our view, the statutory safe harbor should cover forward-looking statements about certain known trends and uncertainties, off-balance sheet arrangements, and aggregate contractual obligations, which must be provided in an IPO registration statement in response to the SEC's MD&A rules. However, in our view, any expansion of the statutory safe harbor for forward looking statements should not extend to an IPO by an ineligible issuer, subject to our comments above on the proposed definition.

Were the SEC to expand the statutory safe harbor in this manner, an eligible non-reporting issuer would be provided equal and appropriate protection in its registration statement with respect to SEC-mandated disclosures of forward-looking statements, which would qualify for safe harbor protection once the registration statement becomes effective and the company becomes a reporting issuer. However, such a limited expansion of the statutory safe harbor would respect the concerns about potential abuse that led Congress to exclude IPOs from the original scope of the statutory safe harbor. With sufficient experience under the statutory safe harbors, and given the SEC's emphasis on the quality and usefulness of MD&A (as expressed in FR-72, *Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations)*, we encourage the SEC to extend the statutory safe harbor to forward-looking statements required to be disclosed within the IPO registration statement.

Further, in connection with the IPO of any issuer, the SEC should not require financial projections, whether or not accompanied by an attestation report from an independent registered public accounting firm. Notwithstanding the Commission's view in Item 10(b) of Regulation S-K, which encourages the use of financial projections in registration statements and certain Exchange Act reports, in our view, because there is no requirement for reporting issuers to file financial projections either in a registration statement or in an Exchange Act report, the Commission should not mandate such a requirement in an IPO registration statement by a non-reporting issuer.

In addition, in Release No. 33-5362, *Statement by the Commission on the Disclosure of Projections of Future Economic Performance*, the Commission expressed "strong reservations about the ability of issuers with limited resources or operational histories to make reasonably based projections." We concur that non-reporting issuers are less likely to have a reasonable basis for making projections, and we question why mandatory projections in IPO registrations statements ever would be appropriate. However, if the SEC ever mandated projections by all issuers, any such projection in an IPO registration statement also should be subject to the statutory safe harbor for the reasons expressed above.

Proposed Amendments to Forms S-1 and F-1

We concur with the Commission's proposed amendments to Forms S-1 and F-1, which would allow reporting issuers, other than ineligible issuers, to incorporate by reference into Form S-1 or Form F-1 their disclosures from previously filed Exchange Act reports. (See our related comments as to the proposed definition of an ineligible issuer.)

In light of universal EDGAR filing by reporting issuers and near universal access of investors to EDGAR filings via the Internet, we concur that the "all-inclusive" prospectus currently required by Forms S-1 and F-1 is no longer necessary. Because the proposed amendments would only allow for "backwards incorporation," we concur that as long as a reporting issuer is current in its Exchange Act reporting obligations, there should be no need for the issuer to have timely filed its Exchange Act reports for the preceding 12 months in order to be eligible to incorporate by reference into its Form S-1 or F-1.

As proposed, eligibility to use incorporation by reference would be conditioned on the issuer making its Exchange Act reports readily accessible on its website. While it is a best practice for companies to provide such access on their websites, it should not be a condition for incorporation by reference. In light of the broad public access to reporting issuers' EDGAR filings on the SEC's website, we support an "access equals delivery" concept with respect to the information incorporated by reference, without separately requiring redundant access on the issuer's own website.

The proposing release indicates that the SEC intended to limit eligibility to use incorporation by reference to reporting issuers that, among other things, had filed at least one annual report. However, we note that the corresponding proposed instruction in Forms S-1 and F-1 states, "The registrant has filed an annual report required under Section 13(a) or 15(d) of the Exchange Act for its most recently completed fiscal year." We would interpret the proposed language to preclude incorporation by reference in Forms S-1 and F-1 that become effective between a reporting issuer's fiscal year end and the date it files its annual report on Form 10-K or Form 20-F. Because this does not appear to be consistent with the SEC's express intention, we suggest that the SEC modify the instruction accordingly.

We also concur with the Commission's proposed elimination of Forms S-2 and F-2. In light of the Commission's proposal that would permit incorporation by reference in Forms S-1 and F-1 without any requirement to deliver the incorporated material, Forms S-2 and F-2, which currently require such delivery, would become unnecessary.

Form S-3 Eligibility

Given that the Commission's proposed amendments to Form S-1 would permit incorporation by reference, the benefit of Form S-3 largely would be limited to delayed or continuous offerings of securities (i.e., eligibility for shelf registration). Currently, an issuer is eligible to use Form S-3 to register any class of securities if, among other things, it has at least $75 million in public voting and nonvoting common equity float, measured as of any date within 60 days of the filing date. The Commission has requested comment on whether it should raise the Form S-3 eligibility threshold of $75 million, which has been in place since 1992. We concur that it would be appropriate to adjust the $75 million eligibility threshold in light of the increase in market equity valuations since 1992. In addition, the SEC should consider adopting an indexing approach, which would provide for periodic adjustments to the threshold based on changes in broad equity market indices. Finally, we recommend that Form S-3 eligibility should not be available to an ineligible issuer, subject to our comments above on the proposed definition.

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We would be pleased to discuss our comments with the Commission or its staff at your convenience.

Very truly yours,

Ernst & Young LLP