

IN THE MATTER OF  
THE NATIONAL DOLLAR STORES, LTD.

*File No. 3-1212. Promulgated September 11, 1968*

Securities Exchange Act of 1934—Section 12(h)

**EXEMPTION FROM REGISTRATION OF OVER-THE-COUNTER  
SECURITIES**

Where issuer applied for conditional exemption of its common stock from registration under Section 12(g) of Securities Exchange Act of 1934, principally on basis of limited number of shareholders who were United States residents and limited trading interest in stock, *held*, sufficient showing had not been made to warrant an exemption as sought, which would also have effect of exempting issuer and its insiders from reporting, proxy and insider trading provisions, but under all the circumstances it is not inconsistent with public interest or protection of investors to exempt applicant, subject to conditions, from requirements of periodic and other reports and certain financial information in registration statement.

**APPEARANCES:**

*Richard D. Maltzman* and *Melvyn I. Mark*, of Eisner & Titchell, for the National Dollar Stores, Ltd.

*Alan B. Levenson*, *W. Stevens Tucker*, *Irving D. Borochoff*, *Norman Cohen* and *Jeffrey B. Schwartz*, for the Division of Corporation Finance of the Commission.

**FINDINGS AND OPINION OF THE COMMISSION**

We have before us an application by The National Dollar Stores, Ltd. ("applicant"), pursuant to Section 12(h) of the Securities Exchange Act of 1934 ("Act"), for a conditional exemption of its common stock from the registration requirements of Section 12(g) of the Act. As pertinent here, Section 12(g), which was added to the Act in 1964, requires an issuer with assets exceeding \$1 million and a class of equity security not listed on a national securities exchange and held of record by at least 500 persons to register such security with us.<sup>1</sup> Registration subjects

<sup>1</sup> These coverage criteria became effective on July 1, 1966, following an initial two-year period in which 750 securityholders was the cutoff point.

the issuer to the reporting and proxy provisions of Sections 13 and 14 of the Act and its insiders to the insider trading provisions of Section 16. Under Section 12(b) of the Act we may grant an exemption from Section 12(g) or from Sections 13, 14 or 16, "upon such terms and conditions and for such period as [we deem] necessary or appropriate," if we find that "by reason of the number of public investors, amount of trading interest in the securities, the nature and extent of the activities of the issuer, income or assets of the issuer, or otherwise, that such action is not inconsistent with the public interest or the protection of investors."

Following hearings, the hearing examiner issued an initial decision denying the application. We granted applicant's petition for review, applicant filed a brief in support of the petition and our Division of Corporation Finance a reply brief, and we heard oral argument. Our findings are based on an independent review of the record.

Applicant, a California corporation, operates a chain of 47 department stores and in addition owns real estate and securities. As of January 31, 1967, it had total assets of about \$12.4 million and a net worth of about \$8.8 million. During the five years ended January 31, 1967, applicant's annual sales ranged between about \$10 million and \$12 million, and its annual net income between about \$242,000 and \$598,000 or about \$24 and \$59 per share, and it paid annual dividends of either \$16 or \$20 per share.

Applicant has 10,000 shares of common stock outstanding. Aside from a few shares held in applicant's treasury, these shares were held as of January 31, 1967, by 599 shareholders of record, of whom 456 were residents of the United States. The shares were originally sold in an offering in 1928 and 1929, principally to members of the Chinese community in the San Francisco area. Applicant's founder and his family acquired about 50 percent of the stock at that time and the family still holds approximately the same amount, principally through a family investment company which owns 4,770 shares and is the only shareholder owning more than 10 percent of the outstanding stock. As to the remaining shares, 11 shareholders owned 100 shares or more and 466 shareholders owned 5 shares or less, including 220 who owned 1 share each and 133 who owned 2 shares each.

Applicant's shares have been traded infrequently. In the 10-year period from 1957 through 1966, a total of 84 sales, involving 404 shares, were effected. None of these transactions involved securities brokers. Under a practice which has been in effect for many

years, stockholders wishing to sell shares have contacted applicant, which has found a buyer, generally among its employees. The sales price has tended to remain constant for several years at a time and in recent years has been \$200 or \$250 per share. No brokers or members of the public have indicated any interest in dealing in or purchasing applicant's stock. In 1967 applicant offered to purchase shares from its stockholders at \$250 per share in order to "fund" a stock option granted to its new president and to reduce the number of shareholders below 500 so as to avoid the need for registration under Section 12(g). Only 19 stockholders accepted the offer, however, tendering a total of about 140 shares which were purchased by applicant.

Applicant has in recent years sent to its shareholders, prior to the annual meeting, an annual report listing applicant's officers and directors, summarizing past activities and future plans, and including certified financial statements. Prior to the 1967 annual meeting applicant also solicited proxies for the election of directors and the granting of stock options to its president and three other officers. Following the hearings applicant modified the request for an unconditional exemption from registration which its application as filed had presented, by proposing that the exemption be subject to certain conditions, including the prompt transmission to us for our public records of copies of annual reports and other communications sent by applicant to its shareholders, expansion in specified respects of the disclosures made to shareholders in annual reports and proxy material, reporting to us of any change in the material facts, and expiration of the exemption in ten years. Applicant urges that such an exemption is warranted in view of the limited number of stockholders who are United States residents, the limited trading interest in its stock, the disclosures which it has made and would make under the proposed conditions and the additional costs involved in registration and the attendant requirements.

In order to place the exemption application and applicant's contentions in their proper context, we summarize briefly the provisions and requirements as to which an exemption is sought. Registration under Section 12(g) which, as noted above, also renders applicable the provisions of Sections 13, 14 and 16, is effected by the filing of a registration statement containing financial statements and other specified information. Form 10, the basic registration form, requires information concerning, among other things, the issuer's business and property, the identity of its officers, directors and principal shareholders and the interests of such persons in material transactions of the issuer, the remunera-

tion of officers and directors, options to purchase the issuer's securities and the number of shareholders. In addition, the issuer must file certified financial statements including profit and loss data for its last three fiscal years and complying with our Regulation S-X. That Regulation, among other things, specifies various supporting schedules to be filed, including schedules with respect to marketable securities, property, plant and equipment, and reserves for depreciation.

In order to keep the information in the registration statement current, Section 13 of the Act and our rules and regulations thereunder require the filing of reports on Forms 10-K, 9-K and 8-K, which in substance update the matters covered in the registration statement.<sup>2</sup> Pursuant to Section 14 of the Act, we have adopted proxy rules and regulations which require an issuer soliciting proxies from its stockholders to make disclosure to them, through a proxy statement which is examined by our staff prior to its use and filed with us, of relevant facts to insure a vote on an informed basis. Soliciting material concerning an election of directors must include information respecting the nominees' identity, occupational background and stockholdings (of the issuer's stock), management compensation in any form, and material interests of officers, directors or principal stockholders in corporate transactions. Moreover, together with or prior to the proxy statement, stockholders must be furnished with an annual report containing certified financial statements. Where proxies are solicited with respect to matters other than the election of directors, disclosures pertinent to the particular matter or matters to be acted upon must be made. Prior to any stockholders' meeting as to which an issuer does not solicit proxies, it must transmit to its stockholders and file with us an information statement containing substantially equivalent information to that required in a proxy solicitation statement, and, if directors are to be elected, an annual report.

Section 16 of the Act, which is designed to curb the improper use of inside information by corporate officials, requires officers, directors and principal shareholders to file reports with us disclosing their holdings of the issuer's stock and changes in such holdings, and provides for recovery from such persons of short-swing trading profits. Also pertinent to our discussion here is Section 18 of the Act, which subjects to civil liability persons who make false

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<sup>2</sup> The Form 10-K report is an annual one which includes certified financial statements complying with Regulation S-X. The Form 9-K report is a semi-annual report consisting of certain uncertified financial data. Specified events or developments must be reported, on Form 8-K, by the tenth of the month following their occurrence.

or misleading statements in any document filed with us pursuant to the Act or any rule or regulation thereunder.

It is apparent that the conditions proposed by applicant regarding disclosures to be made and the transmission of material to us would not provide an adequate substitute for the statutory and regulatory requirements and mechanisms.<sup>3</sup> Nor can we agree that the limited number of domestic stockholders of applicant or the limited trading interest in applicant's stock warrant an exemption on the terms proposed by applicant. Section 12(g) draws no distinction between domestic and foreign securityholders, and its legislative history makes it clear that residence is immaterial to the number-of-securityholders criterion.<sup>4</sup> And while we have recognized that the securities acts are designed primarily to protect the interests of American investors<sup>5</sup> and an exemption from Section 12(g) might be appropriate where such interests are *de minimis*, that is decidedly not the case here where applicant's 456 domestic shareholders represent a significant as well as the major interest.<sup>6</sup> Moreover, while trading interest is undoubtedly an important factor in measuring the significance of the public investor interest,<sup>7</sup> its small scale does not detract from the need of applicant's existing and potential shareholders for at least the principal protections provided through registration under Section 12(g).<sup>8</sup> And

<sup>3</sup> The Report of the Senate Banking and Currency Committee on the 1964 amendments pointed out that while many companies which would be covered by the legislation did make adequate disclosures to their shareholders, "the extent of the public interest in companies with over \$1 million of assets and 500 or more shareholders requiring (sic) strong assurance that the information disclosed by them is, and will continue to be, current, adequate, and susceptible to comparative evaluation," and that this could be achieved only "by requiring disclosure under statutory sanctions and subject to examination by an independent agency for compliance with accounting and other disclosure standards." S. Rep. No. 379, 88th Cong., 1st Sess. 13 (1963).

<sup>4</sup> Applicant, citing *American Banana Co. v. United Fruit Co.*, 213 U. S. 347 (1909), argues that it is a rule of statutory construction that all legislation is *prima facie* territorial and therefore speaks with reference to persons and acts within the geographical boundaries of the country. Whatever the nature of that doctrine, however, it is clearly inapposite here where the issue is whether a domestic company should be required to perform duties in the United States pursuant to statutory requirements, particularly in light of the legislative intent regarding the coverage of Section 12(g) as reflected in the legislative history referred to above.

<sup>5</sup> See e.g., "Registration of Foreign Offerings by Domestic Issuers; Registration of Underwriters of Foreign Offerings as Broker-Dealers," Securities Act Release No. 4708 (July 9, 1964).

<sup>6</sup> By way of comparison, we note that other provisions of the Act and of our rule thereunder indicate that 300 or more shareholders represent a significant public interest. Under Section 12(g)(4), registration of a class of security may be terminated by the issuer if the number of holders has fallen to less than 300, and the same cut-off point is specified with respect to the reporting provisions in Section 15(d). Rule 12g3-2 exempts from registration under Section 12(g) those foreign issuers which have less than 300 securityholders resident in the United States.

<sup>7</sup> See Report of Special Study of Securities Markets, Part 3, pp. 18, 23(1963).

<sup>8</sup> We cannot agree with applicant's contention that since the various criteria listed in Section 12(h), including "amount of trading interest in the securities," are listed in the disjunctive, proof that any one of the criteria exists is sufficient to support a finding that an exemption is "not inconsistent with the public interest or the protection of investors." As we construe the section, the criteria are designed merely to provide us with guidelines in considering the basic tests contained in the last quoted phrase. In any event, Section 12(h) provides for partial as well as blanket exemptions and lack of a trading market is in our view relevant to exemption from Section 13 which as stated below we grant herein.

the fact that it has been applicant's practice to act as intermediary for persons seeking to sell shares and to offer such shares to employees does not make unnecessary disclosures of facts relevant to informed investment decisions by both the sellers and buyers.<sup>9</sup>

We recognize, however, that in view of the absence of a continuing or professional market interest with respect to applicant's stock, the financial community which seeks out and disseminates to the investing public pertinent information filed with us would not in this instance be served by the filing of the periodic and supplemental reports required under Section 13. We have concluded that while it is not appropriate to exempt applicant from registration it would not be inconsistent with the public interest or the protection of investors under the circumstances to grant applicant an exemption from the reporting requirements of Section 13(a) and our rules and regulations thereunder.<sup>10</sup> We note in this connection that the proxy or information statement to be filed with us will contain certified financial statements and other information that must be disclosed in a Form 10-K annual report. Consistent with the above exemption, we also consider it appropriate to permit applicant, in lieu of the financial statements and supporting schedules which it would otherwise be required to file as part of the Section 12(g) registration statement, to file its already existing certified balance sheet as of the end of its latest fiscal year and certified profit and loss data for the latest three years.

Under this disposition, applicant, subject to the qualification stated above, will be required to register its stock under Section 12(g), and applicant and its insiders, respectively, will be subject to the requirements or provisions of Sections 14, 16 and 18.<sup>11</sup> This approach, in our view, takes appropriate cognizance of the interest of applicant's present and potential shareholders and at the same time gives recognition to the historically and potentially limited extent of any sales of applicant's stock and relieves applicant of requirements which would entail additional expense to it without commensurate benefits to investors.

<sup>9</sup> Cf. *S.E.C. v. Ralston Purina Company*, 346 U. S. 119 (1953).

<sup>10</sup> Subsequent to the oral argument in these proceedings, Sections 13 and 14 of the Act were amended by the addition of Sections 13(d) and (e) and 14(d) through (f). Those provisions relate among other things to the purchase by an issuer of its securities during the pendency of a tender offer by others, solicitations respecting such offers, and the replacement of a majority of the directors of an issuer in specified situations. No reason appears why applicant should be exempted from these provisions.

<sup>11</sup> In its petition for review and at the oral argument applicant indicated that if a conditional exemption as proposed by it was not acceptable to us, it would be willing in addition to comply with our proxy rules and regulations, to make full disclosure of insider trading, and to subject itself, with respect to any documents filed with or submitted to us, to the civil liability provisions of Section 18 of the Act.

Consistent with a suggestion made by applicant, our order herein will provide that the financial statements included in applicant's annual reports to shareholders which will be certified in accordance with generally accepted accounting principles will be deemed to be incorporated by reference in its proxy or information statements, so as to make the provisions of Section 18 applicable with respect to them. In addition, the order will include a condition requiring applicant, when acting as middleman between seller and buyer, to furnish any person to whom shares are offered with a copy of the most recent proxy or information statement and annual report. The order also will require applicant to inform us annually of all sales that have been effected in its stock and to advise us promptly of any material change in the facts recited in this opinion, and we will reserve jurisdiction to reconsider the exemption in the event of such a change, or in the event that changes take place in our rules and regulations relating to disclosures by Section 12(g) companies.

An appropriate order will issue.

By the Commission (Chairman COHEN and Commissioners OWENS, BUDGE, WHEAT and SMITH).