



# Federal Register

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**Tuesday,  
June 26, 2007**

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## **Part III**

# **Securities and Exchange Commission**

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**17 CFR Part 239**

**Revisions to the Eligibility Requirements  
for Primary Securities Offerings on  
Forms S-3 and F-3; Proposed Rule**

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Part 239

[Release No. 33-8812; 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:** Proposed rule.

**SUMMARY:** We are proposing to amend the eligibility requirements of Form S-3 and Form F-3 to allow 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 and do not sell more than the equivalent of 20% of their public float in primary offerings pursuant to the new instructions on these forms 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 proposal would not extend to shell companies, however, which would be prohibited from using Form S-3 and Form F-3 for primary offerings until 12 calendar months after they cease being shell companies.

**DATES:** Comments should be received on or before August 27, 2007.

**ADDRESSES:** Comments may be submitted by any of the following methods:

#### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/proposed.shtml>);
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number S7-10-07 on the subject line; or
- Use the Federal Rulemaking Portal (<http://www.regulations.gov>). Follow the instructions for submitting comments.

#### Paper Comments

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-1090.

All submissions should refer to File Number S7-10-07. This file number should be included on the subject line

if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/proposed.shtml>). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

**FOR FURTHER INFORMATION CONTACT:** Daniel Greenspan, at (202) 551-3430, in the Division of Corporation Finance, U.S. Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-3010.

**SUPPLEMENTARY INFORMATION:** We are proposing to amend Form S-3<sup>1</sup> and Form F-3<sup>2</sup> under the Securities Act of 1933.<sup>3</sup>

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

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

<sup>3</sup> 15 U.S.C. 77a *et seq.*

## I. Discussion

### A. Background

#### 1. 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 1934<sup>4</sup> to satisfy the form's disclosure requirements. Although there have been amendments to Form S-3 since it was first adopted in 1982,<sup>5</sup> the basic framework still remains. To use Form S-3, a company must meet the form's registrant requirements,<sup>6</sup> which generally pertain to reporting history under the Exchange Act,<sup>7</sup> as well as at least one of the form's transaction requirements.<sup>8</sup> These transaction requirements provide that companies may 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," is a certain size.<sup>9</sup> 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 that the company has a minimum public float.<sup>10</sup>

#### 2. 1992 Amendments to Form S-3

As originally adopted, the "public float" requirement for companies eligible to use Form S-3 to register primary offerings was \$150 million.<sup>11</sup> In 1992, the Commission reduced the minimum float threshold to the current \$75 million, based on its analysis of the trading markets and market following of registrants in various capitalization

<sup>4</sup> 15 U.S.C. 78a *et seq.*

<sup>5</sup> Most notably, the Commission adopted a set of comprehensive amendments in 2005 known as "Securities Offering Reform." See *Securities Offering Reform*, Release No. 33-8591 (Jul. 19, 2005) (70 FR 44722). See also *Simplification of Registration Procedures for Primary Securities Offerings*, Release No. 33-6964 (Oct. 22, 1992) [57 FR 48970], which is discussed further at n. 12.

<sup>6</sup> See General Instruction I.A. of Form S-3.

<sup>7</sup> For example, the form is available only to issuers that have complied with the reporting requirements of the Exchange Act for at least one year. However, issuers of investment grade asset-backed securities do not need to have a reporting history. See General Instruction I.A.4. of Form S-3.

<sup>8</sup> See General Instruction I.B. of Form S-3.

<sup>9</sup> General Instruction I.B.1. of Form S-3.

<sup>10</sup> See General Instructions I.B.2. through I.B.4. of Form S-3.

<sup>11</sup> *Adoption of Integrated Disclosure System*, Release No. 33-6383 (Mar. 3, 1982) [47 FR 11380].

ranges.<sup>12</sup> When it reduced the required public float to \$75 million, the Commission stated that a large majority of the companies that would become eligible to use Form S-3 for primary offerings as a result of the reduction in required float had securities traded on either a national securities exchange or authorized for inclusion on the NASDAQ National Market System<sup>13</sup> and that approximately two-thirds of the companies were followed by at least three research analysts.<sup>14</sup> This, combined with the success of the 10-year-old integrated disclosure system and shelf registration process, persuaded the Commission that it could extend the benefits of Form S-3 for primary offerings to a larger class of issuers without compromising the investing public's access to sufficient and timely information about such issuers.<sup>15</sup>

### 3. Advisory Committee on Smaller Public Companies

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"), an advisory committee chartered by the Commission in 2005 to assess the current regulatory system for smaller companies under U.S. securities laws.<sup>16</sup> In its April 23, 2006 Final Report to the Commission, the Advisory Committee recommended that we allow all reporting companies listed on a national

securities exchange, NASDAQ or trading 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>17</sup> The Advisory Committee noted that many smaller public companies currently are not eligible to use Form S-3 to register primary offerings because they do not meet the minimum public float requirement and are, therefore, not able to take advantage of the efficiencies associated with the use of the form. As a consequence, the Advisory Committee argued that this restriction placed limits on the ability of such companies to raise capital. The Advisory Committee also expressed its view that the reporting obligations of smaller public companies, combined with the widespread accessibility over the Internet of documents filed with the Commission, have lessened the need to retain the public float standard in Form S-3. In the Advisory Committee's view, the Exchange Act reporting obligations of smaller public companies are comparable today to even the largest reporting companies and, therefore, compliance with these disclosure requirements "should be sufficient to protect investors and inform the marketplace about developments in these companies."<sup>18</sup>

### 4. Reasons for Proposal

The ability to conduct primary offerings on Form S-3 confers significant advantages on eligible companies. 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 as well as those that will be filed in the future.<sup>19</sup> The ability

of Form S-3 registrants to incorporate their subsequently filed Exchange Act reports, often called "forward incorporation," allows for automatic updating of the registration statement. By contrast, a registrant without the ability to forward incorporate<sup>20</sup> must file a new registration statement or post-effective amendment to its registration statement to prevent information in the registration statement from becoming outdated and to update for fundamental changes to the information set forth in the registration statement.<sup>21</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>22</sup> Rule 415 provides considerable flexibility in accessing the public securities markets from time to time in response to changes in the market and other factors. Companies that are eligible to register these primary "shelf" offerings under Rule 415 are permitted to register securities offerings prior to planning any specific offering and, once the registration statement is effective, offer securities in one or more tranches without waiting for further Commission action. In general, post-effective amendments and new registration statements may be subject to selective review by the Commission staff and must be declared effective by the Commission or our staff through delegated authority before the registration statement may be used again to offer and sell securities.<sup>23</sup> The shelf eligibility resulting from Form S-3 eligibility and the ability to forward incorporate on Form S-3, therefore, allow companies to avoid additional

<sup>12</sup> Release No. 33-6964. In that release, the Commission estimated that, as a result of the reduction in required float, 450 additional companies with an aggregate float of \$88 billion would be eligible to register primary offerings of their securities on Form S-3. This is compared to the Commission's estimate, in Release No. 33-6943, of 370 companies that registered approximately \$200 billion of securities on Form S-3 for delayed primary shelf offerings during calendar year 1991.

As part of this rulemaking, the Commission also reduced the reporting history necessary to register on Form S-3 from 36 to 12 months for most issuers and eliminated the alternative eligibility test for primary offerings requiring registrants to have a public float of at least \$100 million and an annual trading volume of at least 3 million shares.

<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 for conversion from a national securities association to a national securities exchange. The NASDAQ Stock Market commenced operations on August 1, 2006.

<sup>14</sup> *Simplification of Registration Procedures for Primary Securities Offerings*, Release No. 33-6943 (July 16, 1992) [57 FR 32461], at p. 6. In this discussion, the Commission stated that "one indicia of market interest and following of a company is the number of research analysts covering the company."

<sup>15</sup> *Id.*

<sup>16</sup> More information about the Advisory Committee is available at <http://www.sec.gov/info/smallbus/acspc.shtml>.

<sup>17</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.

<sup>18</sup> The Final Report, at 69. The Advisory Committee also noted:

The Sarbanes-Oxley Act has required more frequent SEC review of periodic reports as well as enhanced processes, such as disclosure controls and procedures and certifications by the chief executive and chief financial officers, which further enhance investor protection.

*Id.* at 70.

<sup>19</sup> See Item 12 of Form S-3: "Incorporation of Certain Information by Reference."

<sup>20</sup> For example, Forms S-1 and SB-2 do not allow registrants to forward incorporate their Exchange Act filings.

<sup>21</sup> See Section 10(a)(3) of the Securities Act (requiring that the information contained in a prospectus used more than nine months after the effective date be as of a date not more than sixteen months prior to the effective date) and Item 512(a)(1)(i) and (ii) of Regulation S-K (requiring the inclusion by the company of an undertaking to file a post-effective amendment to comply with Section 10(a)(3) of the Securities Act and to reflect the occurrence of facts or events arising after the effective date that, individually or in the aggregate, represent a fundamental change in the information set forth in the registration statement).

<sup>22</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>23</sup> See Section 8(c) of the Securities Act.

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>24</sup>

Registration of an offering on Form S-1, the form available to many companies ineligible to use Form S-3, permits certain issuers<sup>25</sup> to incorporate by reference previously filed Exchange Act reports, but it does not permit registrants to automatically update information in the prospectus by forward incorporation of their Exchange Act filings. Further, issuers filing registration statements on Form S-1 because they are not eligible to file on Form S-3 are not permitted to register primary shelf offerings under Rule 415. Thus, it is harder for Form S-1 registrants to take advantage of favorable market opportunities. Consequently, we believe that extending Form S-3 short-form registration to additional issuers should enhance their ability to access the public securities markets.

Given the great advances in the electronic dissemination and accessibility of company disclosure transmitted over the Internet over the last several years,<sup>26</sup> we believe that

<sup>24</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>25</sup> See General Instruction VII. to Form S-1, "Eligibility to Use Incorporation by Reference," for the criteria that registrants on Form S-1 must meet in order to incorporate information by reference.

<sup>26</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

expanding the class of companies that are permitted to use Form S-3 for primary securities offerings is once again warranted. In contrast to 1992, when the Commission last adjusted the issuer eligibility requirements for Form S-3,<sup>27</sup> all filings on Form S-3 now are filed on the Commission's Electronic Data Gathering, Analysis and Retrieval system ("EDGAR") and, therefore, are available at little or no cost to anyone interested in obtaining the information. While we believe that retaining some restrictions on Form S-3 eligibility is still advisable, we nevertheless agree with the Advisory Committee that more companies should benefit from the greater flexibility and efficiency in accessing the capital markets afforded by Form S-3. Accordingly, we are proposing to amend the Form S-3 eligibility requirements to permit registrants other than shell companies to use Form S-3 for primary offerings, whether or not they satisfy the minimum \$75 million float threshold, so long as they stay within certain offering size limitations and otherwise satisfy the eligibility requirements of the form, such as timely Exchange Act reporting for at least the prior year.

#### B. Proposed Revisions to Form S-3

Specifically, we are proposing 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>28</sup> provided:

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>27</sup> See Release No. 33-6964.

<sup>28</sup> As mentioned in n. 17 above, 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 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 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 Sheet issuers. Notwithstanding the Advisory Committee's recommendation, we are not at this time proposing to amend the Form S-3 eligibility rules for secondary offerings because of the potential for abusive primary offerings disguised as secondary offerings. As such, this rulemaking proposal pertains only to 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. In this regard, we also are not revising the interpretive positions on secondary offering eligibility under General Instruction I.B.3.

- They meet the other registrant eligibility conditions for the use of Form S-3;<sup>29</sup>

- They are not shell companies<sup>30</sup> and have not been shell companies for at least 12 calendar months before filing the registration statement; and

- They do not sell more than the equivalent of 20% of their public float in primary offerings under General Instruction I.B.6. of Form S-3 over any period of 12 calendar months.<sup>31</sup>

As a result, even companies not traded on a national securities exchange could potentially avail themselves of this new eligibility rule so long as they were able to satisfy the registrant eligibility requirements provided in General Instruction I.A.<sup>32</sup> This would include companies quoted on the Over-the-Counter-Bulletin Board and Pink Sheets quotation services. We note that the Over-the-Counter-Bulletin Board requires quoted issuers to be registered

<sup>29</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 Section 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 Section 12 or 15(d) of the Exchange Act and has filed in a timely manner all the material required to be filed pursuant to Section 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.

<sup>30</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).

<sup>31</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 proposed General Instruction I.B.6. of Form S-3, if a registrant relies on this Instruction to conduct a shelf takedown equivalent to 20% 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>32</sup> Form S-3 eligibility under proposed General Instruction I.B.6 and Form F-3 eligibility under proposed General Instruction I.B.5. is not intended to have broader implications under our rules beyond an issuer's ability to conduct a 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 those proposed additional 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). See Instruction 6 to proposed General Instruction I.B.6. of Form S-3 and Instruction 6 to proposed General Instruction I.B.5. of Form F-3.

under Section 12 of the Exchange Act<sup>33</sup> and filing Exchange Act reports or otherwise filing periodic reports with the appropriate regulatory agency. Moreover, we have built into our proposed rule the condition that an eligible company must be required to file Exchange Act reports and has timely filed all such reports for the 12 calendar months and any portion of a month preceding the filing of the registration statement.

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 proposal contemplates 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 20% limitation would be exceeded.

The proposal would require 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>34</sup> Then, for purposes of calculating the aggregate market value of securities sold during the preceding period of 12 calendar months, the proposal would require that registrants add together the gross sales price for all primary offerings pursuant to proposed Instruction I.B.6. to Form S-3 during the preceding period of 12 calendar months. Based on that calculation, registrants would be permitted to sell securities with a value up to, but not greater than, the difference between 20% of their public float and the value of securities sold in

primary offerings on Form S-3 under proposed Instruction I.B.6. in the prior period of 12 calendar months.<sup>35</sup> We have placed the cap of 20% in order to allow an offering that is large enough to help an issuer meet its financing needs when market opportunities arise but small enough to take into account the effect such new issuance may have on the market for a thinly traded security.

This aggregate gross sales price includes the sales of equity as well as debt offerings. Therefore, these registrants would now be eligible to offer non-investment grade debt on Form S-3.<sup>36</sup> In the case of securities that are convertible into or exercisable for equity shares, such as convertible debt or warrants, however, we are proposing 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 would 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 proposed General Instruction I.B.6. of Form S-3. We believe calculating the 20% 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 proposed 20% limit on sales is not intended to impact a holder's ability to convert or exercise derivative securities purchased from the company. For example, the 20% limit would apply to the amount of common stock warrants that a company could sell under Form S-3, and the number of common shares into which the warrants are exercisable would be relevant for determining the company's compliance with the 20%

<sup>35</sup> As proposed, the method of calculating the 20% limit on sales is the same whether the registrant is selling equity or debt securities, or a combination of both. If the proposed 20% limitation excluded debt, there is some concern that we would be inadvertently encouraging issuances of debt securities over equity. Because we do not intend for the rule to dictate or otherwise influence the overall form of security that companies offer, we have drafted the 20% limit on sales to include both equity and debt.

<sup>36</sup> Currently, registrants may offer non-convertible investment grade debt securities on Form S-3 regardless of the size of their public float. See General Instruction I.B.2. to Form S-3.

rule at the time the warrants were sold, but would not impede the purchaser's later exercise of the warrants.

Consistent with our desire to ensure that the expansion of Form S-3 eligibility does not diminish the protection of investors, the proposal specifically excludes 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>37</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>38</sup> Under the proposal, a former 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:

- 12 calendar months after it ceases being a shell company;
- Has filed information that would be required in a registration statement on Form 10, Form 10-SB or Form 20-F, as applicable, to register a class of securities under Section 12 of the Exchange Act; and
- Has been timely reporting for 12 calendar months.<sup>39</sup>

<sup>37</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 proposed 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>38</sup> See, for example, Release No. 33-8591; Release No. 33-8587; *Delayed Pricing for Certain Registrants*, Release No. 33-7393 (Feb. 20, 1997) [62 FR 9276]; and *Penny Stock Definition for Purposes of Blank Check Rule*, Release No. 33-7024 (Oct. 25, 1993) [58 FR 58099].

<sup>39</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, Form 10-SB or Form 20-F, as applicable, to register a class of securities under Section 12 of the Exchange Act. See 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 proposed new provisions of S-3 and F-3 until at least 12

<sup>33</sup> 15 U.S.C. 78l.

<sup>34</sup> The determination of public float is based on a public trading market for the registrant's common equity. This is the same requirement in General Instruction I.B.1. of Form S-3 and Form F-3 that a registrant have a \$75 million market value and in the definition of accelerated filer in Exchange Act Rule 12b-2 [17 CFR 240.12b2]. Therefore, an entity with common equity securities outstanding but not trading in any public trading market would not be entitled to sell securities in a primary offering on Form S-3 under this proposal. Note that the determination of public float for purposes of form eligibility in current General Instruction I.B.1 of Form S-3 is based on the price of the registrant's common equity within 60 days prior to the date of filing the registration statement. The determination of "aggregate market value" for purposes of determining an issuer's status as an accelerated filer under Rule 12b-2 is based on the market price of the issuer's equity as of the last business day of the issuer's most recently completed second fiscal quarter.

Ordinarily, this information would be filed in a current report on Form 8-K reporting completion of the transaction that causes it to cease being a shell company.<sup>40</sup> In other cases, the information may be filed in a Form 10, Form 10-SB or Form 20-F. Consistent with the current registrant eligibility rules of Form S-3 and Form F-3 that require at least 12 calendar months of timely reporting, the proposed 12 calendar-month delay is intended to provide investors in the former shell company with the benefit of 12 full months of disclosure in the newly structured entity prior to its use of Form S-3 or Form F-3 for primary securities offerings.

As proposed, the 20% limitation is designed to allow issuers flexibility. Because the restriction on the amount of 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 20% 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 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 20% of the float decreases from the time the registration statement was initially filed, would not necessarily run afoul of the 20% limitation because the relevant point in time for determining whether a registrant has exceeded the threshold would be 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 20% of the registrant's float calculated within 60 days of the sale, then the transaction

calendar months after it ceases being a shell company.

<sup>40</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 or Form 10-SB to register a class of securities under Section 12 of the Exchange Act.

would not violate proposed 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 20% of the new lower float.<sup>41</sup>

Because Form S-3 registrants who meet the \$75 million float threshold of 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, we believe it is appropriate to provide issuers registering on Form S-3 pursuant to proposed 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 proposing an instruction to I.B.6. that lifts the 20% restriction on additional sales in the event that the registrant's float increases to \$75 million or more subsequent to the effective date. Of course, pursuant to Rule 401, registrants would also be 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 20% restriction would be reimposed for all subsequent sales made pursuant to General Instruction I.B.6. and would remain in place until the registrant's float equaled or exceeded \$75 million.

The following examples illustrate how the proposed Instruction would operate.<sup>42</sup> For purposes of these examples, we are assuming that the hypothetical registrants satisfy the registrant eligibility requirements in

<sup>41</sup> Along these lines, under the proposal registrants would be able to sell up to the equivalent of the full 20% of their public float immediately following the effective date of their registration statement, provided that there were no prior sales pursuant to proposed 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 in registration statement. See Release No. 33-8591. Assuming that the sale of the entire 20% allotted under the proposal complied with the rule at the time of the takedown, the subsequent contraction in the registrant's public float would not invalidate this prior sale.

<sup>42</sup> The examples that follow are for illustrative purposes only and are not intended to be indicative of market activity.

General Instruction I.A. of Form S-3 and are not shell companies.

#### *Example A*

On January 1, 2008, a registrant with a public float of \$50 million files a shelf registration statement on Form S-3 pursuant to proposed General Instruction I.B.6. intending to register the registrant's offer and sale of up to \$20 million of debt and equity securities over the next three years from time to time as market opportunities arise.<sup>43</sup> The registration statement is subsequently declared effective. In March 2008, 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 proposed General Instruction I.B.6. Calculating that its public float is now \$55 million, the registrant determines that the total market value of all sales effected pursuant to Instruction I.B.6. over the past year, including the intended sale, may not exceed \$11 million, or 20% of the registrant's float. Since the registrant has not previously filed on Form S-3 and has made no prior sales off the subject Form S-3, it is able to sell the entire \$11 million off the subject Form S-3.

Assuming that it sold the entire \$11 million of securities in March 2008, the registrant in September 2008 once again contemplates a takedown off the shelf. It determines that its public float (as calculated pursuant to Instruction 1 to proposed General Instruction I.B.6.) has risen to \$60 million. Because 20% of \$60 million is \$12 million, the registrant is now able to sell additional securities in accordance with proposed General Instruction I.B.6(a), even though in March 2008 it took down the equivalent of what was then the entire 20% of its float. However, because the registrant has already sold \$11 million worth of its securities within the 12 calendar months prior to the contemplated sale, the registrant may sell no more than \$1 million of additional securities at this time.

In December 2008, the registrant determines that its public float has risen to \$85 million. To this point, assuming it has only sold an aggregate of \$12 million of its securities pursuant to the subject Form S-3 as described above, it has \$8 million of securities remaining

<sup>43</sup> Although only 20% of the public float may be sold in any year, a company may register a larger amount.

on the registration statement and potentially available for takedown (the total amount registered of \$20 million, less the \$12 million previously sold). Because 20% of \$85 million is \$17 million, and the registrant has already sold \$12 million within the previous year, Instruction I.B.6.(a) would, in most circumstances, prohibit the registrant from selling more than an additional \$5 million of securities in the latest offering. However, under Instruction 3 to proposed General Instruction I.B.6., the registrant is no longer subject to the 20% limitation on annual sales because its float has exceeded \$75 million. If it chooses, the registrant may sell the entire remaining \$8 million of securities all at once or in separate tranches at any time until the company updates the registration statement pursuant to Section 10(a)(3) by filing a Form 10-K. This will be the case even if the registrant's float subsequently falls below \$75 million until it files that Form 10-K.

#### Example B

A registrant has 12 million shares of voting common equity outstanding held by nonaffiliates. The market price of this stock is \$5, 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 proposed 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 proposed 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 at \$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, the value of the securities being offered for purposes of General Instruction I.B.6. is \$11,111,110 (2,222,222 shares at \$5 per share), which is less than the \$12 million allowed by the 20% cap (20% 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 proposed 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<sup>44</sup> prior to the anticipated sale by the per share market price of the registrant's equity used for purposes of determining its current float.

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 proposed 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 is then multiplied by the current market value of \$5.55. Thus, for purposes of Instruction 2 to proposed General Instruction 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 would 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 year. If this amount is less than 20% of the registrant's current public float, it may sell additional securities with a value up to, but not greater than, the difference between 20% of its current public float and the value of all securities sold by it pursuant to Instruction I.B.6. during the preceding year.

#### Example C

A registrant has an effective registration statement on Form S-3 through which it intends to conduct shelf offerings of its securities. The Form S-3 was filed pursuant to proposed General Instruction I.B.6. At the time of its first shelf takedown, the registrant's public float is equal to \$20 million (which means that the maximum amount available to be sold under the 20% cap would be \$4 million). Based on proposed General Instruction I.B.6(a), the registrant sells \$3 million available of its debt securities. Six months later, the registrant's public float has decreased to \$10 million. The registrant wishes to conduct an additional takedown 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 \$10 million, General Instruction I.B.6(a) would only allow the registrant to sell a maximum of \$2 million worth of securities (20% of \$10 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 proposed General Instruction I.B.6.) at \$3 million in the 6 months prior to the contemplated sale and so must wait until at least a full year has passed since the \$3 million sale of debt securities to undertake another offering off the Form S-3 unless its float increases. Note that, although the registrant's float would not allow additional sales, the \$3 million takedown of securities 6 months prior does not violate the 20% restriction because, at the time of that prior sale, the registrant's float was \$20 million.

Because allowing smaller public companies to take advantage of shelf primary offerings on Form S-3 would permit such companies to avail themselves of periodic takedowns

<sup>44</sup> Note that 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 proposed General Instruction I.B.6. See Instruction 5 to proposed General Instruction I.B.6.

without further Commission action or prior staff review, some concerns have been raised.<sup>45</sup> Although the Commission staff may review registration statements before they are declared effective, individual takedowns are not subject to prior selective staff review. Under the current rules, if these issuers were instead using Form S-1 or Form SB-2, they would be required to file separate registration statements for each new offering, which would be subject to pre-offering selective staff review before going effective.

While we recognize that extending the benefits of shelf registration to an expanded group of companies will, by necessity, limit the staff's direct prior involvement in takedowns of securities off the shelf, we believe that the risks will be justified by the benefits that will accrue by facilitating the capital formation efforts of smaller public companies. As we have discussed elsewhere in this release, the risks to investor protection by expanding the base of companies eligible for primary offerings on Form S-3 have been significantly mitigated by technological advances affecting the manner in which companies communicate with investors, allowing widespread, direct, and contemporaneous accessibility to company disclosure at little or no cost. Moreover, the scope of disclosure

<sup>45</sup> For example, see *Report of the Task Force on Disclosure Simplification* (Mar. 5, 1996) (the "Task Force"), available at <http://www.sec.gov/news/studies/smpl.htm>. Among other things, the Task Force 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.

See also, *Delayed Pricing for Certain Registrants*, Release No. 33-7393 (Feb. 20, 1997) [62 FR 9276]. Following on the Task Force's recommendations, the Commission proposed to permit certain smaller companies to price registered securities offerings on a delayed basis for up to one year after effectiveness. The Commission noted, however:

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.

obligations and liability of smaller public companies under the federal securities laws are sufficiently comparable for these purposes to the largest reporting companies such that the proposed expansion of Form S-3 primary offering eligibility should not adversely impact investors.<sup>46</sup>

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. Securities in thinly traded markets may be more vulnerable to potential manipulative practices. In this regard, to ensure that shelf eligibility is expanded with appropriate moderation and attention to the continued protection of investors, we have proposed to exclude shell companies from eligibility and to impose a 20% restriction on the amount of securities that can be sold into the market on Form S-3 in any period of 12 calendar months by issuers with a public float below \$75 million.<sup>47</sup> By placing such restrictions on the expansion of Form S-3 eligibility, we believe we are mitigating the potential for abuse that could result as a function of the increase in the volume of smaller public company securities sold in primary offerings on Form S-3. At the same time, we believe that the 20% limit will be sufficient to accommodate the capital raising needs of the large majority of smaller public companies.<sup>48</sup>

<sup>46</sup> We acknowledge that the companies implicated in this rulemaking are not yet 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 Financial Reporting Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934*, Release No. 34-55929 (June 20, 2007).

<sup>47</sup> Under the proposal, offerings above the 20% limitation would violate the form requirements, and may have implications under Section 5.

<sup>48</sup> In connection with this rulemaking, the Division of Corporation Finance undertook a review of shelf registration takedowns in 2006 by companies with a public float of moderate size. 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 suggests that limiting smaller public companies to 20% of their public float in any 12-month period strikes the appropriate balance between the capital

We note that the Advisory Committee, in its May 2006 Final Report to the Commission, expressed support for a more expansive rule change, with no suggestion of a limitation on Form S-3 eligibility other than current required Exchange Act reporting and listed on a national securities exchange or the Over-the-Counter Bulletin Board. However, we are not at this time proposing such a less restrictive eligibility requirement. We believe that by restricting the applicability of the revised eligibility rule to companies that are not shell companies and by imposing the 20% limitation on the amount of securities that smaller public companies may sell pursuant to primary offerings on Form S-3, as described, the proposal strikes the appropriate balance between helping to facilitate capital formation through the securities markets and our objective of investor protection. If the amendment is adopted as proposed, this would not foreclose the possibility that we may revisit the appropriateness of this 20% restriction at a later time. However, we believe that limiting the expanded use of S-3 as proposed will allow us to consider the impacts of the expansion in an environment where there are limitations so that investor protection concerns are addressed.

### C. Proposed Revisions to Form F-3

Form F-3, which was designed to parallel Form S-3,<sup>49</sup> is the equivalent short-form registration form available for use by "foreign private issuers" <sup>50</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

needs of these companies and investor protection concerns.

<sup>49</sup> See *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>50</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.



form's transaction requirements.<sup>51</sup> The Form F-3 registrant requirements are similar to Form S-3 and generally relate to a registrant's reporting history under the Exchange Act.<sup>52</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>53</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 digested and disseminated to the marketplace. When the Commission adopted Form F-3 in 1982,<sup>54</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>55</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>56</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>57</sup>

<sup>51</sup> See General Instruction I. of Form F-3: "Eligibility Requirements for Use of Form F-3."

<sup>52</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) 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), at 2 (explaining that the requirement was adopted "in order to ensure that information regarding the issuer is available to the market").

<sup>53</sup> See 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>54</sup> *Adoption of Foreign Issuer Integrated Disclosure System*, Release No. 33-6437 (Nov. 19, 1982) [47 FR 54764].

<sup>55</sup> See Release No. 33-7029, at 2.

<sup>56</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>57</sup> Release No. 33-7029, at 2.

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 by domestic issuers on Form S-3 without compromising investor protection.<sup>58</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>59</sup> we are proposing amendments to Form F-3 that are comparable to our proposed changes to Form S-3. Specifically, proposed General Instruction I.B.5. to Form F-3 would 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;
- They are not shell companies and have not been shell companies for at least 12 calendar months before filing the registration statement; and
- They do not sell more than the equivalent of 20% of their public float in primary offerings under General Instruction I.B.5. on Form F-3 over any period of 12 calendar months.

#### D. Request for Comment

We request and encourage any interested person to submit comments on the proposal and any other matters that might have an impact on the proposal. With respect to any comments, we note that such comments are of greatest assistance to our rulemaking initiative if accompanied by supporting data and analysis of the issues addressed in those comments. In addition to general comment, we encourage commenters to address the following specific questions:

<sup>58</sup> In the release adopting this change to the Form F-3 eligibility requirements, 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>59</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.

• Is the proposed change in the public float eligibility criteria for Forms S-3 and F-3 appropriate? Is our assumption correct that it is appropriate to lift the public float restrictions in a limited manner given advances in the electronic dissemination and accessibility of company disclosure transmitted over the Internet?

• In this regard, in what way is market following an important criteria in light of these technological changes?<sup>60</sup>

• The Form S-3 eligibility requirement for primary offerings which requires minimum public float was last set in 1992 at \$75 million. Based on the Personal Consumption Expenditures Price Index (PCEPI) and the Consumer Price Index (CPI), if this threshold were adjusted for inflation, it would equal between \$100-110 million, respectively, in today's dollars. Does this suggest that we should not adopt this proposal and leave the form eligibility requirements unchanged, since by retaining \$75 million as the minimum and not raising it to at least \$100 million to account for inflation, we are in effect allowing a lower threshold than was established in 1992?

• Should the Commission retain the float test in all cases for primary offerings, but set it below \$75 million? Should the float test be higher than \$75 million?

• Should we make parallel changes to Forms S-3 and F-3, as proposed? If not, in what way should they be different? For example, are there special conditions relating to foreign issuers that would make any of the proposed amendments not appropriate or should they be tailored in any way?

• Is there a more appropriate criteria to determine eligibility for primary offerings on Forms S-3 and F-3 than public float? Given the more limited liquidity of companies with a public float less than \$75 million, would a more appropriate criteria for eligibility relate to Average Daily Trading Volume for the prior year? If so, is 25% of Average Daily Traded Volume an appropriate cap (for ADTV) per year? Should the cap be based on dollar volume traded per day? If not, how would the criteria be evaluated for purposes of determining issuances other than common stock? If Average Daily Trading Volume is used as the criteria instead of public float, over what period should the average be calculated?

• Is the proposed 20% limitation on the amount of securities that can be sold

<sup>60</sup> See Release No. 33-6383, at 8 (discussing the objective of relating short-form registration to the existence of widespread following in the marketplace).

over any period of 12 calendar months appropriate? Should this restriction be broader or more narrow? For example should 20% be higher or lower or should the one-year period be longer or shorter? Is this the right amount to provide smaller public companies with a realistic financing alternative? If the restriction is not appropriate as proposed, what alternatives are preferable and why?

- Proposed General Instruction I.B.6. of Form S-3 would restrict the amount of securities that can be sold by a registrant over a period of "12 calendar months." This parallels the way in which the phrase "12 calendar months" is used for purposes of the registrant eligibility requirements in Form S-3. Therefore, if a registrant relies on General Instruction I.B.6. to conduct a shelf takedown equivalent to 20% 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. Instead of "12 calendar months," would it be preferable if the relevant measurement period was "one year," so that a registrant who conducted a shelf takedown equal to 20% of its float on September 15, 2007 would next be eligible to do another takedown (assuming no change in its float) under General Instruction I.B.6. on September 15, 2008?

- Should we allow non-investment grade debt to be offered under this provision? Should we have a cap for the amount of non-investment grade debt that may be sold? If so, is it appropriate to tie the cap to public float? If not, what would be a more appropriate criteria?

- In the case of securities that are convertible into or exercisable for equity shares, such as convertible debt securities, we are proposing that the registrant calculate the amount sold by reference to the aggregate market value of the underlying equity shares in lieu of the market value of the convertible securities. Should we also include in the amount the value of the overlying securities? Should derivative securities be calculated in a different manner?

- Under Rule 430B, except for an effective date resulting from the filing of a form of prospectus for purposes of updating the registration statement pursuant to Section 10(a)(3) or reflecting fundamental changes in the information in the registration statement pursuant to the issuer's undertakings, the prospectus filing will not create a new effective date for directors or signing officers of the issuer, whereas the filing of a registration statement on Form S-1, which issuers with a market capitalization of less than \$75 million

would otherwise need to use for these offerings, would. Likewise, the filing of the prospectus will not be a new effective date for auditors who provided consent in an existing registration statement for their report on previously issued financial statements as the filing of a new Form S-1 would. Is this potential "gap" in liability appropriate in the situations allowed under the proposed revisions?

- Should the 20% limitation be calculated only with respect to securities sold pursuant to the proposed amendment or should it include all securities sold pursuant to registered public offerings on Form S-3, S-1, SB-2, etc.? Should the 20% also include securities sold pursuant to private offerings? Should it include securities sold pursuant to registered public offerings on any form by selling shareholders?

- Should the calculation of 20% of the registrant's public float reflect increases and decreases in the registrant's public float during the period that its shelf registration statement is effective, as is currently proposed? Do concerns relating to investor protection and potential market manipulation weigh in favor of a different method of calculating the 20% limitation, such as determining the 20% limit at the time the registration statement is filed rather than at the time of each sale under the registration statement? Would an annual limitation on the number of offerings on Forms S-3 and F-3 that a registrant may conduct under proposed General Instruction I.B.6. strike the appropriate balance between investor protection and capital formation facilitation?

- Should the calculation of a registrant's public float for purposes of the amendment be based on an average, such as the average weekly float during the four calendar weeks preceding the sale in question?

- As proposed, General Instruction I.B.6. of Form S-3 and General Instruction I.B.5. of Form F-3 provide that the 20% restriction on sales will be lifted in the event that the registrant's public float equals or exceeds \$75 million subsequent to the effective date. However, registrants would be required to recompute their public float each time they filed an amendment to update the registration statement pursuant to Rule 401 and, if the float measured less than \$75 million, the 20% restriction on sales could be reimposed until the float equaled or exceeded \$75 million. If the 20% restriction is lifted because the registrant's public float surpasses \$75 million, but is subsequently reimposed because the float falls below \$75

million, should the calculation of 20% take into consideration the value of all securities sold pursuant to Form S-3 (or Form F-3, as applicable) in primary offerings in the preceding year; only securities sold pursuant to General Instruction I.B.6. of Form S-3 (or General Instruction I.B.5. of Form F-3, as applicable), in the preceding year; or, should the calculation ignore the value of securities sold prior to the date of the update when the float was last measured?

- In the event that a registrant's public float equals or exceeds \$75 million, is it appropriate for the transformation of the filing from a primary shelf filing under General Instruction I.B.6. of Form S-3 (or General Instruction I.B.5. of Form F-3, as applicable) to a primary shelf filing under General Instruction I.B.1. of Form S-3 (or General Instruction I.B.1. of Form F-3, as applicable) to be made without there being a new effective date for the registration statement? If we should have a new effective date for the registration statement, how would that date be set and should there be any filing made with the Commission?

- Should the calculation of a registrant's public float for purposes of the amendments be made by reference to the price of the registrant's common equity within 60 days prior to the date of sale, or should the reference period for the price of the registrant's common equity be as of a date closer to the date of sale?

- What should be the consequence of an issuer exceeding the 20% restriction on sales? If the consequences of violating the 20% are significant, would the risks of doing so adversely affect the willingness of issuers to use the proposal? If so, what, if anything, should be done to ameliorate those risks?

- Should the issuer's intent be a factor in determining the consequences of a violation of the 20% restriction?

- Should we amend Rule 401(g)<sup>61</sup> of the Securities Act to provide that violations of the 20% restriction would also violate the requirements as to proper form under Rule 401 even though the registration statement has been declared effective previously?

- The proposal does not exclude any type of offerings, such as at-the-market offerings. Should we impose restrictions on the manner of sale under proposed General Instruction I.B.6. to Form S-3 (and, on Form F-3, proposed General Instruction I.B.5.), so that only certain kinds of distributions, such as firm

<sup>61</sup> 17 CFR 230.401(g).

commitment underwritten offerings, are permitted?

- We recently eliminated restrictions on primary “at-the-market” offerings of equity securities for primary shelf eligible issuers because we felt they were not necessary to provide protection to markets or investors for seasoned issuers.<sup>62</sup> Given that the proposal allows smaller companies to do primary offerings, should registrants utilizing proposed General Instruction I.B.6. to Form S-3 (and, on Form F-3, proposed General Instruction I.B.5.) be prohibited from conducting at-the-market offerings under Rule 415(a)(4)?<sup>63</sup> If at-the-market offerings are allowed, should we nevertheless require that such offers and sales be made only through registered broker-dealers and require such broker-dealers to be named as underwriters in the prospectus?

- Should all companies with a public trading market, including companies traded on the Pink Sheets, be allowed to use the amended form as proposed or should we limit it to just interdealer quotations systems with some level of oversight and operated by a self-regulatory organization?

- Is the proposal not to extend expanded Form S-3 and F-3 eligibility to shell companies appropriate? If not, why?

- Are there other restraints on the proposed expansion of Form S-3 and F-3 eligibility that should be considered, such as restricting the classes of issuers that may utilize this expansion or the types and amounts of securities that

may be registered on Forms S-3 and F-3 pursuant to this expansion?

- If the eligibility standards for Form S-3 and Form F-3 are expanded as proposed, will allowing this larger class of companies to conduct limited primary offerings of their securities on these forms provide them with a meaningful source of financing? How might this proposal impact the private markets for these companies’ securities?

- If the proposal is adopted, what types of financings are issuers likely to make on the expanded eligibility on Form S-3 and F-3?

- If the proposal is adopted, it is foreseeable that some companies with a public trading market but with securities not listed or authorized for listing on a national securities exchange may be eligible to offer such securities in primary offerings on Form S-3 or Form F-3. Since the proposal is not intended to alter the exemption from state regulation of securities offerings under Section 18 of the Securities Act, will the effect of state blue sky law make it prohibitively difficult for companies without “covered” securities (as defined by Section 18(b)) to register such securities in primary offerings on Form S-3 and F-3 pursuant to the proposal? If the answer is yes, what steps can we take to make the amendments more useful to companies?

- Are there any market practices that may arise as a result of this proposal that we should be concerned about?

- Is there any investor protection loss the proposal does not address? If so, how can we address it? Are there any additional disclosures that are appropriate? For instance, are there any disclosures required in Forms S-1 or F-1 that should be included in Forms S-3 or F-3 filed under General Instruction I.B.6. of Form S-3 or General Instruction I.B.5. of Form F-3, respectively? Should issuers have to disclose in the prospectus their calculation of the amount of securities being offered, the amount offered pursuant to these Instructions for the last 12 calendar months and of the amount of securities that may be offered under the filing during the year?

## II. Paperwork Reduction Act

### A. Background

The proposed amendments to Forms S-3 and F-3 contain “collection of information” requirements within the meaning of the Paperwork Reduction Act of 1995.<sup>64</sup> We are submitting these to the Office of Management and Budget for review and approval in accordance

with the Paperwork Reduction Act.<sup>65</sup> The titles for this information are:

“Form S-3” (OMB Control No. 3235-0073);  
 “Form S-1”<sup>66</sup> (OMB Control No. 3235-0065);  
 “Form SB-2”<sup>67</sup> (OMB Control No. 3235-0418);  
 “Form F-3” (OMB Control No. 3235-0256); and  
 “Form F-1”<sup>68</sup> (OMB Control No. 3235-0258)

We adopted existing Forms S-3, S-1, SB-2, 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 proposed amendments to Forms S-3 and F-3 are intended to allow issuers that are currently 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 and meet the other eligibility requirements of the forms.

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, SB-2, 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 proposing in this release pertain only to Forms S-3 and F-3 eligibility and not to the disclosure required by these forms, we do not believe that the amendments will impose any new

<sup>62</sup> See Release No. 33-8591.

<sup>63</sup> Prior to the adoption of Securities Offering Reform in July 2005, Rule 415 prohibited registrants from making at-the-market offerings on Form S-3 or Form F-3 unless certain conditions were met. The conditions were that: The amount of securities could not exceed ten percent of the registrant’s public float; the securities had to be sold through an underwriter or underwriters acting as principal(s) or agent(s) for the registrant; and the underwriter(s) must be named in the prospectus. Among other things, the 2005 amendments eliminated these restrictions for primary shelf eligible issuers. In the Securities Offering Reform adopting release, the Commission stated:

The restrictions on primary “at-the-market” offerings of equity securities currently set forth in Rule 415(a)(4) were adopted initially to address concerns about the integrity of trading markets. As discussed in the Proposing Release, we are eliminating these restrictions for primary shelf eligible issuers because they are not necessary to provide protection to markets or investors. The market today has greater information about seasoned issuers than it did at the adoption of the “at-the-market” limitations, due to enhanced Exchange Act reporting. Further, trading markets for these issuers’ securities have grown significantly since that time. Requiring the involvement of underwriters and limiting the amount of securities that can be sold imposes artificial limitations on this avenue for these issuers to access capital.

Release No. 33-8591, at 213-214.

<sup>64</sup> 44 U.S.C. 3501 *et seq.*

<sup>65</sup> 44 U.S.C. 3507(d) and 5 CFR 1320.11.

<sup>66</sup> Because our amendments to Form S-3 and Form F-3 are anticipated to affect the annual number of Forms S-1, Forms SB-2 and Forms F-1 filed, we are required to include them in the titles of information collections even though we are not proposing to amend them in this release.

<sup>67</sup> See n. 66 above.

<sup>68</sup> *Id.*

recordkeeping or information collection requirements. On a per-response basis, this proposal would 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, SB-2 or F-1, as applicable, we believe there will be an aggregate decrease in the disclosure burdens associated with Forms S-1, SB-2 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, SB-2 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, SB-2 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 Form S-3. We also anticipate that many companies will choose to offer their securities directly to the public through registration on Forms S-3 and F-3 instead of through private placements and therefore, if the proposal is adopted, we expect comparatively more Form 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 proposed amendments to Forms S-3 and F-3 will result in an overall increase in the number of such forms filed annually and an overall decrease in the number of Forms S-1, Forms SB-2 and Forms F-1 filed annually. 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, Forms SB-2 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 proposal would result in a net increase in the annual aggregate number of filings on all Forms S-3, S-1, SB-2, 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, SB-2 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, SB-2 or F-1. However, this offset could be lessened in part by the proposed 20% limitation on the amount of securities that companies may sell on Form S-3 and Form F-3 in any period of 12 calendar months. Companies that require more capital but are prohibited by this 20% restriction 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, SB-2 or F-1 or through the private markets even though Form S-3 and F-3 are preferable.

#### *C. Paperwork Reduction Act Burden Estimates*

For purposes of the Paperwork Reduction Act, we estimate the annual decrease in the paperwork burden for companies to comply with our proposed collection of information requirements to be approximately 39,952 hours of in-house company personnel time and to be approximately \$47,942,000 for the services of outside professionals.<sup>69</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 mentioned, however, the estimated decreases are wholly attributable to our assumptions, discussed in Section 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>70</sup> or Form F-3,<sup>71</sup> as applicable, but had a public float of less than \$75 million at the end of their last fiscal year. In all, we estimate that there were 4,901 such companies at the end of calendar year 2006 and that they filed a total of 815 registration statements on Forms S-1, SB-2 and F-1 during the twelve months ending December 31, 2006.<sup>72</sup> To determine the effect of our proposal on the overall paperwork burden, we have assumed that these filings on Forms S-1, SB-2 and F-1 would have been made instead on Form S-3 or Form F-3, as applicable, to the extent that the issuers would not be limited by the proposed 20% restriction on the amount of securities they may offer in any period of 12 calendar months. Therefore, we assume that the Forms S-1, SB-2 and F-1 filed by the subject companies will decrease from the number filed in 2006, but because of the proposed 20% restriction on sales, will not decrease to 0. Instead, we believe that some Forms S-1, SB-2 and F-1 will continue to be filed annually by these companies. To reflect this, we have taken the number of Forms S-1, SB-2 and F-1 that were filed by these companies in calendar year 2006 and decreased this number by 85% for each form, for a total decrease of 694 filings.<sup>73</sup> Therefore, we assume that approximately 694 fewer Forms S-1, SB-2 and F-1 will be filed by all issuers in calendar year 2006. The actual number could be more or less depending on various factors, including future market conditions.

Furthermore, we believe that the 4,901 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, either did not file registration statements on Forms S-1 SB-2 or F-1, or were limited in the number that they

<sup>70</sup> See n. 29 above.

<sup>71</sup> See n. 51 above.

<sup>72</sup> The total of 815 filings is comprised of 138 Forms S-1; 674 Forms SB-2; and 3 Forms F-1.

<sup>73</sup> This number deducts 85% from the totals for each of the three registration forms, as follows: Form S-1 (85% of 138, rounded up, equals 118); Form SB-2 (85% of 674, rounded up, equals 573); and Form F-1 (85% of 3, rounded up, equals 3). Adding these together, the combined reduction totals 694 filings.

<sup>69</sup> For administrative convenience, the presentation of 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.

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 694 fewer registration statements on Forms S-1, SB-2 and F-1 that we estimate will be filed going forward by the 4,901 companies who would qualify for primary offerings on Forms S-3 and F-3 as a result of our proposal. We further assume that this increase in Forms S-3 and F-3 will be mitigated to some degree by the proposed 20% restriction on securities sold in any period of 12 calendar months, which may limit the frequency and volume of additional securities offerings on Form S-3 and Form F-3. To reflect this, we have taken the 694 Forms S-1, SB-2 and F-1 that were filed by these companies in calendar year 2006 and increased this number by 10% for each

form, for a total increase of 765 filings.<sup>74</sup> Therefore, we assume that approximately 765 additional Forms S-3 and F-3 will be filed over and above the number of total Forms S-3 and F-3 filed by all issuers, large and small, in calendar year 2006. The actual number could be more or less depending on various factors, including future market conditions.

To calculate the total effect of the proposed amendments on the overall compliance burden for all issuers, large and small, we subtracted the burden associated with the 694 fewer Forms S-1, SB-2 and F-1 registration statements that we expect will be filed annually in the future and added the burden associated with our estimate of 765 additional Forms S-3 and F-3 filed annually as a result of the proposal. 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>75</sup> we estimate that 25% of the burden of preparation of Forms S-3, S-1, SB-2, 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>76</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, SB-2, F-3 and F-1 as a result of this proposal.

Form	Estimated change in annual responses (A)	Hours/form <sup>77</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 .....	761	459	349,299	87,324.75	261,974.25	\$104,789,000
S-1 .....	(118)	1,176	(138,768)	(34,692)	(104,076)	(41,630,400)
SB-2 .....	(573)	638	(365,574)	(91,393.5)	(274,180.5)	(109,672,200)
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)
Total .....	.....	.....	(159,806)	(39,951.5)	(119,854.5)	(47,941,800)

#### D. Request for Comment

We request comment in order to evaluate the accuracy of our estimate of the burden of the collections of information.<sup>78</sup> Any member of the public may direct to us any comments concerning the accuracy of these burden estimates. Persons who desire to submit comments on the collection of information requirements should direct their comments to the OMB, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should send a copy of the comments to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-1090, with reference to File No. S7-10-07.

<sup>74</sup> This number adds a 10% premium to the individual totals for each of the three registration forms, as follows: Form S-1 (10% of 118, rounded up, equals 12); Form SB-2 (10% of 573, rounded up, equals 58); and Form F-1 (10% of 3, rounded up, equals 1). The sum of these increases, which is equal to 71, is then added to the total of 694 Forms S-1, SB-2 and F-1 filed by the subject companies in 2006.

Requests for materials submitted to the OMB by us with regard to this collection of information should be in writing, refer to File No. S7-10-07, and be submitted to the Securities and Exchange Commission, Office of Filings and Information Services, Branch of Records Management, 6432 General Green Way, Alexandria, VA 22312. Because the OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication, your comments are best assured of having their full effect if the OMB receives them within 30 days of publication.

<sup>75</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>76</sup> In connection with other recent rulemakings, we have had discussions with several private law

### III. Cost-Benefit Analysis

#### A. Summary of Proposals

We are proposing revisions to the transaction eligibility requirements of Forms S-3 and F-3 that would 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 current instructions to Forms S-3 and F-3 restrict 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 propose to allow companies with

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>77</sup> This reflects current Office of Management and Budget estimates.

<sup>78</sup> Comments are requested pursuant to 44 U.S.C. 3506(c)(2)(B).

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 are not shell companies and have not been shell companies for at least 12 calendar months before filing the registration statement; and
- They do not sell more than the equivalent of 20% 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 over any period of 12 calendar months.

#### 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, F-1 and SB-2.<sup>79</sup> This difference is magnified by the fact that Form S-3 and Form F-3, unlike Forms S-1, SB-2 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 amendments to the registration statement.

Overall, we anticipate that the proposed 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, Form SB-2 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 proposal the annual decrease in the compliance burden for companies to comply with our proposed collection of information requirements to be approximately 39,952 hours of in-house company personnel time (valued at \$6,992,000<sup>80</sup>)

<sup>79</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, F-1 and SB-2 as 1,176 hours, 1,809 hours and 638 hours, respectively.

<sup>80</sup> Consistent with recent rulemaking releases, we estimate the value of work performed by the company internally at a cost of \$175 per hour.

and to be approximately \$47,942,000 for the services of outside professionals. If our assumptions regarding these costs and current practices are not correct or complete, then the decreased costs we anticipate may prove to be either higher or lower than our current estimate.

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, SB-2 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, as we have proposed, will facilitate the capital-raising efforts of smaller public companies who currently have fewer financing options than their larger counterparts.<sup>81</sup> Consequently, we anticipate that the proposal, if adopted, would 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

<sup>81</sup> See generally, Chaplinsky and Haushalter, *Financing Under Extreme Uncertainty: Contract Terms and Returns to Private Investments in Public Equity*.

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>82</sup>

The public registration of securities also provides additional benefits to investors over alternative forms of capital raising. To the extent that the amendments, if adopted, lead to an increase in the use of Form S-3 and Form F-3 as a source of financing and a 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 proposed 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 proposed 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 20% sales restriction 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>83</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, SB-2 or F-1, they would be required to file separate registration statements for each new offering, which

<sup>82</sup> *Id.*

<sup>83</sup> See n. 45 above.

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 in 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 the benefits of the rule.

While we recognize that extending the benefits of shelf registration to an expanded group of companies will, by necessity, 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 costs will be justified by the benefits that will accrue by facilitating the capital formation efforts of smaller public companies. As we have discussed elsewhere in this release, the risks to investor protection by expanding the base of companies eligible for primary offerings on Forms S-3 and F-3 have been significantly mitigated by technological advances affecting the manner in which companies communicate with investors, allowing widespread, direct, and contemporaneous accessibility of company disclosure at little or no cost. Moreover, the scope of heightened disclosure obligations and liability of smaller public companies under the Federal securities laws are sufficiently comparable for these purposes to the largest reporting companies such that the proposed expansion of Form S-3 and Form F-3 primary offering eligibility should not adversely impact investors. In this regard, to ensure that the expansion of eligibility is carried out with appropriate moderation and attention to the continued protection of investors, we have proposed to exclude shell companies from eligibility and to impose a 20% restriction 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 this 20% limitation may be more difficult given the lack of prior staff review before a shelf offering.

#### *D. Request for Comment*

We solicit comments, including quantitative data, to assist our assessment of the costs and benefits of the proposal that we have identified, or any other costs or benefits that we have not addressed but ought to consider. Commenters are encouraged to address any potentially material costs and benefits, whether direct or indirect.

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

Securities Act Section 2(b)<sup>84</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 proposed amendments, if adopted, to increase efficiency and enhance capital formation, and thereby benefit investors, by facilitating the ability of smaller public companies to access the capital markets consistent with investor protection. Currently, many companies are ineligible to use Forms S-3 and F-3 to register primary offerings of their securities because the size of their public float does not satisfy the \$75 million threshold required by these forms. Consequently, they are 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. We believe that 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, in part, for the relative illiquidity of the restricted shares they are purchasing.<sup>85</sup>

We therefore believe that extending shelf registration benefits to more companies as we have proposed will facilitate the capital-raising efforts of smaller public companies who currently have fewer financing options than their larger counterparts.<sup>86</sup> Consequently, we anticipate that the proposal, if adopted, would lead to efficiencies in capital formation, as smaller issuers would 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 in 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

<sup>85</sup> See n. 82.

<sup>86</sup> See n. 81.

<sup>84</sup> 15 U.S.C. 77b(b).

significantly negate the benefits of the rule.

We do not believe that the potential efficiencies and benefits to capital formation resulting from the amendments will be substantially lessened by these potential costs. We believe that the risks to investor protection by expanding the base of companies eligible for primary offerings on Forms S-3 and F-3 have been significantly mitigated by technological advances affecting the manner by which companies communicate with investors, allowing widespread, direct, and contemporaneous accessibility of company disclosure at little or no cost. Moreover, the scope of heightened disclosure obligations and the liability of smaller public companies under the federal securities laws are sufficiently comparable for these purposes to the largest reporting companies, such that the proposed expansion of Form S-3 and Form F-3 primary offering eligibility should not adversely impact investors. In this regard, to provide that the expansion of eligibility is carried out with appropriate moderation and attention to the continued protection of investors, we have proposed to exclude shell companies from eligibility and to impose a 20% restriction 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.

In addition to the salutary effects that we anticipate with respect to capital formation, companies may also realize cost efficiencies stemming from the enhanced ability to incorporate by reference disclosure information from their Exchange Act filings. Because Forms S-3 and F-3 allow a company maximum reliance on its Exchange Act filings to satisfy required prospectus disclosure, these registration statements can be more abbreviated than alternative registration forms and are updated automatically by the company's future Exchange Act filings. This translates into a reduction in the time and the cost of preparing and reviewing disclosure, filing documents, and retaining records. We estimate that under the proposal the annual decrease in the compliance burden for companies who previously were ineligible to use Forms S-3 and F-3 for primary offerings to be approximately 39,952 hours of in-house company personnel time (valued at \$6,992,000<sup>87</sup>) and to be approximately \$47,942,000 for the services of outside professionals.

The effects of the proposed 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 S-3 and 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.

We request comment on whether the proposals, if adopted, would promote efficiency, competition, and capital formation or have an impact or burden on competition. Commenters are requested to provide empirical data and other factual support for their views, if possible.

#### V. Initial Regulatory Flexibility Act Analysis

This Initial Regulatory Flexibility Act Analysis has been prepared in accordance with 5 U.S.C. 603. It relates to proposed 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. Reasons for the Proposed Action

Currently, many smaller public companies are ineligible to use Forms S-3 and F-3 to register primary offerings of their securities because the size of their public float does not satisfy the \$75 million threshold required by these forms. Consequently, they are 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. Objectives

The proposed amendments aim to amend Forms S-3 and F-3 to extend the benefits of incorporation by reference and shelf registration to more companies, which in turn will facilitate the ability of smaller public companies to access the capital markets.

##### C. Legal Basis

We are proposing these amendments pursuant to Sections 6, 7, 8, 10 and 19(a) of the Securities Act, as amended.

##### D. Small Entities Subject to the Proposed Amendments

The Regulatory Flexibility Act defines "small entity" to mean "small business," "small organization," or "small governmental jurisdiction."<sup>88</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>89</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>90</sup>

The proposal would affect small entities that are not shell companies 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>91</sup> Based on these registrant eligibility requirements, we estimate that there are approximately 990 small entities that would be affected by the proposal and would therefore become eligible to use Form S-3 or

<sup>88</sup> 5 U.S.C. § 601(6).

<sup>89</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>90</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. 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>91</sup> See n. 29 and n. 51 above.

<sup>87</sup> See n. 80 above.



Form F-3 for primary securities offerings.

#### *E. Reporting, Recordkeeping and Other Compliance Requirements*

The proposed amendments to the transaction eligibility requirements of Forms S-3 and F-3 would affect only small entities that meet the registrant eligibility requirements of Form S-3 or Form F-3, as applicable, are not shell companies and choose voluntarily to register one or more primary securities offerings on Form S-3 or Form F-3. 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 would decrease their existing compliance burden. Because the proposal does not affect the information disclosure requirements of Form S-3 or Form F-3, we do not believe that the costs of complying with the amendments for small entities will be disproportionate to that of large entities.<sup>92</sup> We recognize, however, that there will be some additional costs associated with an issuer's need to continually monitor its compliance with the proposed 20% limitation 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 proposed collection of information requirements to be approximately 7,854 hours of in-house company personnel time (valued at \$1,375,000<sup>93</sup>) and to be approximately \$9,425,000 for the services of outside professionals. To arrive at these estimates, we applied the same methodology to small entities that we described in Section II.C. above for large and small companies combined. Assuming that 990 small entities would be eligible for primary offerings on Forms S-3 and F-3 if the proposal is adopted, we estimated that these entities filed a total of 193 registration statements on Forms S-1, SB-2 and F-1 during the twelve months ending

<sup>92</sup> It should be noted, however, that General Instruction II.C. of Form S-3 currently requires "small business issuers" (as defined in Rule 405 of the Securities Act [17 CFR 230.405]) to refer to the disclosure items in Regulation S-B [17 CFR 228.10 *et seq.*] and not Regulation S-K. Since Regulation S-B disclosure requirements generally are less extensive than Regulation S-K, small business issuers that file on Form S-3 may have a comparatively lesser compliance burden than larger issuers. However, because the Office of Management and Budget does not provide average compliance estimates for Form S-3 that distinguish

December 31, 2006.<sup>94</sup> We then assumed that these filings on Forms S-1, SB-2 and F-1 would have been made instead on Forms S-3 or Form F-1, as applicable, to the extent that the issuers would not be limited by the proposed 20% restriction on the amount of securities they may offer in any period of 12 calendar months. Therefore, we assume that the Forms S-1, SB-2 and F-1 filed by the subject small entities will decrease from the number filed in 2006 but, because of the proposed 20% restriction on sales, this number will not decrease to 0. Instead, we believe that some Forms S-1, SB-2 and F-1 will continue to be filed annually by these small entities. As such, we have taken the number of Forms S-1, SB-2 and F-1 that were filed by these small entities in calendar year 2006 and decreased this number by 85% for each form, for a total decrease of 165 filings.<sup>95</sup> Therefore, we assume that approximately 165 fewer Forms S-1, SB-2 and F-1 will be filed by all small entities in calendar year 2006. The actual number could be more or less depending on various factors, including future market conditions.

Furthermore, we believe that the 990 small entities 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 small entities 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, 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 165 fewer registration statements on Forms S-1, SB-2 and F-1 that we estimate will be filed going forward by the 990 small entities who would

between filers subject to Regulation S-K and filers subject to Regulation S-B, we have not made such a distinction in this Initial Regulatory Flexibility Analysis.

<sup>93</sup> See n. 80 above.

<sup>94</sup> The total of 193 filings is comprised of 21 Forms S-1; 172 Forms SB-2; and 0 Forms F-1.

<sup>95</sup> This number deducts 85% from the totals for each of the three registration forms, as follows: Form S-1 (85% of 21, rounded up, equals 18); Form SB-2 (85% of 172, rounded up, equals 147); and Form F-1 (85% of 0 equals 0). Adding these

qualify for primary offerings on Forms S-3 and F-3 as a result of our proposal. We further assume that this increase in Forms S-3 and F-3 will be mitigated to some degree by the proposed 20% restriction on securities sold in any period of 12 calendar months, which may limit the frequency and volume of additional securities offerings on Form S-3 and Form F-3. To reflect this, we have taken the 165 Forms S-1, SB-2 and F-1 that were filed by these small entities in calendar year 2006 and increased this number by 10% for each form, for a total increase of 182 filings.<sup>96</sup> Therefore, we assume that approximately 182 additional Forms S-3 and F-3 will be filed over and above the number of total Forms S-3 and F-3 filed by small entities in calendar year 2006. The actual number could be more or less depending on various factors, including future market conditions.

To calculate the total effect of the proposed amendments on the overall compliance burden for small entities, we subtracted the burden associated with the 165 fewer Forms S-1, SB-2 and F-1 registration statements that we expect will be filed annually by small entities in the future and added the burden associated with our estimate of 182 additional Forms S-3 and F-3 filed annually by small entities as a result of the proposal. 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.

We estimate that 25% of the burden of preparation of Forms S-3, S-1, SB-2, F-3 and F-1 is carried by the small entity internally and that 75% of the burden is carried by outside professionals retained by the small entity at an average cost of \$400 per hour. The portion of the burden carried by outside professionals is reflected as a cost, while the portion of the burden carried by the small entity internally is reflected in hours.

The table below illustrates our estimates concerning the incremental annual compliance burden in hours and cost for Forms S-3, S-1, SB-2, F-3 and F-1 for small entities as a result of this proposal.

together, the combined reduction is equal to 165 filings.

<sup>96</sup> This number adds a 10% premium to the individual totals for each of the three registration forms, as follows: Form S-1 (10% of 18, rounded up, equals 2); Form SB-2 (10% of 147, rounded up, equals 15); and Form F-1 (10% of 0 equals 0). The sum of these increases, which is equal to 17, is then added to the total of 165 Forms S-1, SB-2 and F-1 filed by the subject companies in 2006.

<sup>97</sup> This reflects current Office of Management and Budget estimates.

Form	Estimated change in annual responses (A)	Hours/form <sup>77</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 .....	182	459	83,538	20,884.5	62,653.5	\$25,061,400
S-1 .....	(18)	1,176	(21,168)	(5,292)	(15,876)	(6,350,400)
SB-2 .....	(147)	638	(93,786)	(23,446.5)	(70,339.5)	(28,135,800)
F-3 .....	0	166	0	0	0	0
F-1 .....	0	1,809	0	0	0	0
Total .....			(31,416)	(7,854)	(23,562)	(9,424,800)

We encourage written comments regarding this analysis. We solicit comments as to whether the proposed amendments could have an effect that we have not considered. We request that commenters describe the nature of any impact on small entities and provide empirical data to support the extent of the impact.

*F. Duplicative, Overlapping or Conflicting Federal Rules*

We believe that there are no Federal rules that conflict with or completely duplicate the proposed amendments.

*G. Significant Alternatives*

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 proposal, 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 this proposal. Alternative 3 is not applicable, as the distinction between performance standards and design standards has no bearing on the proposed 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 proposal, if adopted, would reduce the compliance burden on eligible smaller entities. Regarding Alternative 4, we considered relaxing the transaction eligibility requirements for Forms S-3 and F-3 to a greater degree than we are

proposing. As discussed above in this release, some have advocated in favor of allowing primary offerings on Form S-3 by all companies that have been reporting under the Exchange Act for at least one year and are current in their Exchange Act reporting at the time of filing. As we stated, however, we decline at this time to propose a less restrictive eligibility requirement. We believe that imposing the 20% limitation on the amount of securities that smaller public companies may sell pursuant to primary offerings on Forms S-3 and F-3, as described, strikes the appropriate balance between helping to facilitate capital formation through the securities markets and our primary objective of investor protection.

*H. Solicitation of Comment*

We encourage the submission of comments with respect to any aspect of this Initial Regulatory Flexibility Analysis. In particular, we request comments regarding:

- The number of small entity issuers that may be affected by the proposed revisions to Forms S-3 and F-3;
- The existence or nature of the potential impact of the proposed revisions on small entity issuers discussed in the analysis; and
- How to quantify the impact of the proposed revisions.

Commenters are asked to describe the nature of any impact and provide empirical data supporting the extent of the impact. Such comments will be considered in the preparation of the Final Regulatory Flexibility Analysis, if the proposed revisions are adopted, and will be placed in the same public file as comments on the proposed amendments.

**VI. Small Business Regulatory Enforcement Fairness Act**

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996,<sup>98</sup> a rule is “major” if it has resulted, or is likely to result in:

- An annual effect on the U.S. economy of \$100 million or more;
- A major increase in costs or prices for consumers or individual industries; or
- Significant adverse effects on competition, investment or innovation.

We request comment on whether our proposal would be a “major rule” for purposes of the Small Business Regulatory Enforcement Fairness Act. We solicit comment and empirical data on:

- The potential effect on the U.S. economy on an annual basis;
- Any potential increase in costs or prices for consumers or individual industries; and
- Any potential effect on competition, investment, or innovation.

**VII. Statutory Authority and Text of the Amendments**

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

**List of Subjects in 17 CFR Part 239**

Reporting and recordkeeping requirements, Securities.

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

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

1. The authority citation for part 239 is revised 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(d), 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.

\* \* \* \* \*

2. 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.

<sup>98</sup> Pub. L. 104-121, Title II, 110 Stat. 857 (1996).

**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 20% of the aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant; and

(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.

**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 20% 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, Form 10–SB, or Form 20–F (§ 249.210, § 249.210b, 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).

\* \* \* \* \*

3. 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 20% of the aggregate market value worldwide of the voting and non-voting common equity held by non-affiliates of the registrant; and

(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.

**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 20% 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, Form 10–SB, or Form 20–F (§ 249.210, § 249.210b, 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.

\* \* \* \* \*

Dated: June 20, 2007.

By the Commission.

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

[FR Doc. E7-12301 Filed 6-25-07; 8:45 am]

**BILLING CODE 8010-01-P**