

THE SEC ADOPTS AMENDMENTS TO FORMS S-3 AND F-3 TO FACILITATE SMALLER COMPANY ACCESS TO CAPITAL MARKETS

January 2, 2008

At its open meeting on December 11, 2007, the Securities and Exchange Commission (the "SEC") adopted¹ amendments (the "Amendments") to the eligibility requirements of Form S-3² and Form F-3³ under the Securities Act of 1933, as amended (the "Securities Act"). The SEC published the adopting release⁴ with the final text of the Amendments on December 19, 2007. The SEC adopted the Amendments substantially as proposed⁵ but with some modifications. The Amendments will allow eligible domestic and foreign private issuers (other than shell companies) that do not meet the current \$75 million public float requirements of the forms to register primary offerings of their securities on the forms, subject to certain restrictions. The Amendments are intended to allow smaller 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 Amendments will take effect on January 28, 2008.

1. See SEC Press Release at <http://www.sec.gov/news/press/2007/2007-259.htm>

2. Form S-3 is a "short-form" registration statement that permits eligible domestic companies to satisfy the form's disclosure requirements by incorporating information from their reports filed under the Securities Exchange Act of 1934 (the "Exchange Act").

3. Form F-3, which was designed to parallel Form S-3, is the equivalent short-form registration statement available for use by foreign private issuers to register securities offerings under the Securities Act. The Form F-3 registrant requirements are similar to those of Form S-3. Unless stated otherwise, references herein to Form S-3 also apply to Form F-3.

4. See Securities Act Adopting Release No. 33-8878 (December 19, 2007) at <http://www.sec.gov/rules/final/2007/33-8878.pdf>

5. See Securities Act Proposing Release No. 33-8812 (June 20, 2007) at <http://www.sec.gov/rules/proposed/2007/33-8812.pdf>

Prior to the Amendments, the registration of primary offerings on Forms S-3 and F-3 was limited to those companies having a public float of \$75 million or more or those companies registering primary offerings of non-convertible investment grade debt or certain other transactions.⁶ The public float requirement precluded many smaller public companies from using Form S-3 to register primary offerings and taking advantage of the efficiencies associated with use of the short form. These advantages include:

- incorporation by reference of previously and subsequently filed Exchange Act reports to satisfy the form's disclosure requirements, allowing for automatic updating of the registration statement. This enables companies to avoid the delays and costs associated with preparing and filing post-effective amendments; and
- use of shelf registration under Rule 415 of the Securities Act,⁷ which allows registrants to have more control over the timing of their offerings, permitting them to raise capital on more favorable terms (such as pricing) or obtain lower interest rates on debt. This gives issuers a significant financing alternative to other available methods, such as private placements with shares

6. The requirements relating to use of Form S-3 for primary offerings of non-convertible investment grade debt or the other transactions have not been amended.

7. Companies that are eligible to register 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, known as "shelf takedowns," without waiting for further SEC action.

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usually priced at a discount based in part on their relative illiquidity.

As amended⁸, the Form S-3 and Form F-3 requirements will allow companies with less than \$75 million in public float to register primary offerings of securities to be sold for cash, provided they:

- meet the other registrant eligibility conditions⁹ for the use of the form;
- are not shell companies¹⁰ and have not been shell companies for at least 12 calendar months before filing the registration statement;¹¹

8. The Amendments will add General Instruction I.B.6 to Form S-3 and General Instruction I.B.5 to Form F-3.

9. To use Form S-3, a domestic company must, among other things:

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

10. Rule 405 under the Securities Act defines a "shell company" as a registrant, other than an asset-backed issuer, that has (a) no or nominal operations and (b) either (1) no or nominal assets, (2) assets consisting solely of cash and cash equivalents or (3) assets consisting of any amount of cash and cash equivalents and nominal other assets. The SEC has clarified that this prohibition applies equally to "blank check companies" as defined in Rule 419 of the Securities Act.

11. Registrants that have been shell companies at any time previously are required to have filed current

- have a class of common equity securities listed and registered on a national securities exchange;¹² and
- do not sell more than the equivalent of one-third¹³ of the aggregate market value of their voting and non-voting common equity held by non-affiliates, or public float, in primary offerings pursuant to the new instruction in any period of 12 calendar months.¹⁴

The Amendments as adopted added the requirement of a class of common equity securities listed and registered on a national securities exchange and changed the cap on the amount of securities that may be sold in any 12-month period from 20% to one-third of the public float.

Form 10 information at least 12 months prior to reflect non-shell company status.

12. Only exchanges registered under Section 6(a) of the Exchange Act will be deemed to be "national securities exchanges" for the purpose of the new General Instruction I.B.6. It should be noted that an exchange that lists or trades security futures products (as defined in Section 3(a)(56) of the Exchange Act) may register as a national securities exchange under Section 6(g) of the Exchange Act solely for the purpose of trading security futures products. However, these Section 6(g) exchanges will not qualify as "national securities exchanges" for the purpose of the new General Instruction.

13. Although only one-third of the public float may be sold in any period of 12 calendar months, a company may register a larger amount on the Form S-3 registration statement.

14. A company's public float has for many years been used as an approximate measure of a stock's market following and, consequently, the degree of efficiency with which the market absorbs information and reflects it in the price of a security. The SEC believes that the reporting obligations of smaller public companies, which are comparable to even the largest reporting companies, combined with the widespread accessibility over the Internet of documents filed with the SEC, should be sufficient to protect investors and inform the marketplace about developments in these companies and have lessened the need to retain the pre-existing public float standard in Form S-3.

The SEC believes that the increase in the cap will allow an offering that is large enough¹⁵ to help an issuer raise a relatively significant amount of capital when market opportunities arise, while the common equity securities listing and registration requirement should provide an additional measure of protection for investors.¹⁶

15. The calculation of the cap is designed to allow issuers flexibility. The restriction on the amount of securities that may be sold over a period of 12 calendar months is calculated by reference to an issuer's public float *immediately prior to a contemplated sale*, as opposed to the time of the initial filing of the registration statement, and, consequently, the amount of securities that an issuer is permitted to sell may continue to grow over time as the issuer's public float increases. Conversely, the amount of securities that an issuer is permitted to sell at any given time may also decrease if the issuer's public float contracts. It is important to note, however, that a contraction in a registrant's float, such that the value of one-third of the public float decreases from the time the registration statement was initially filed, would not run afoul of the 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 one-third of the registrant's public float calculated within 60 days of the sale, then the transaction would not violate the limitation even if the registrant's public float later drops to a level such that the prior sales now account for over one-third of the new lower public float.

16. The exchanges' listing rules and initial and maintenance standards provide an additional measure of protection for investors. An exchange's initial listing standards require listed issuers to possess sufficient public float, investor base and trading interest to assure that the market for the issuer's security has the depth and liquidity necessary to maintain fair and orderly markets. On the other hand, an exchange's maintenance listing criteria help assure that the issuer continues to meet the exchange's standards for depth and liquidity. Generally, listed issuers are required to meet minimum standards relating to number of public shareholders and shares outstanding, shareholder approval of specified matters and, in certain cases, earnings or income. Listed issuers of common equity securities are also required to meet strong corporate governance standards, including the requirement that the issuer's board be composed of a majority of independent directors and that key committees be composed solely of independent directors. Exchange-listed securities also are subject to real-time report-

The Amendments provide the following process for issuers to determine the amount of securities that may be sold:

- determine the value of voting and non-voting common equity held by non-affiliates, using 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 as of a date within 60 days prior to the date of sale; and
- determine the gross proceeds of all sales of all equity and debt securities¹⁷ sold pursuant to the new General Instruction during the 12-month period immediately prior to, and including, the proposed sale.¹⁸

ing of quotation and transaction information, which benefits investors by apprising them of current market information about the security. The SEC believes that these common attributes allow the exchanges to sustain efficient and liquid markets that should help monitor the expansion of shelf registration eligibility on Form S-3 and help mitigate any attendant risks posed by expansion.

17. As adopted, the method of calculating the one-third cap on sales is the same whether the registrant is selling equity or debt securities. Therefore, eligible registrants will also be able to offer non-investment grade debt on Form S-3.

18. In the case of derivative securities, issuers should use the aggregate market value of the underlying equity securities in lieu of the market value of the derivative securities. The market value of the underlying equity securities should be based on the maximum number of shares into which the derivative securities may be converted or for which they may be exercised as of a date within 60 days prior to the date of sale, multiplied by the same per share market price of the issuer's equity used for purposes of calculating the issuer's public float under the first step. If the derivatives have been converted or exercised, issuers should use the actual number of shares received upon conversion or exercise and the market price on the date of conversion or exercise.

It is important to note that the one-third of public float 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 limit

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Issuers will be permitted to sell securities with a value not greater than the difference between one-third of their public float, as determined in the first step, and the value of securities sold in the preceding 12 calendar months, as determined in the second step.¹⁹

Issuers must disclose on the outside front cover of the prospectus the calculation of the aggregate market value of the registrant's outstanding voting and non-voting common equity and the amount of all securities offered pursuant to the new General Instruction during the 12-month period ending on and including the date of the prospectus.

The SEC also adopted a corresponding amendment to Rule 401(g) under the Securities Act.²⁰ The amendment states that violations of the new General Instruction will also violate the requirements as to proper form under Rule 401 even though the registration statement may have previously been declared effective.

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

19. In the adopting release, the SEC pointed out that the one-third cap relates only to primary offerings conducted pursuant to the new General Instruction I.B.6. to Form S-3. Accordingly, an issuer that is temporarily prevented from utilizing Form S-3 for shelf offerings to raise capital would not be foreclosed from registering a primary offering of securities on Form S-1 or selling in private placements.

20. The Amendments add paragraph (g)(3) to Rule 401.

If an issuer's public float equals or exceeds \$75 million subsequent to the effective date of the registration statement, the limitation on sales will not apply to additional sales pursuant to the registration statement. In that case, the registration statement will be deemed to have been filed pursuant to General Instruction I.B.1 instead of the new General Instruction. However, an issuer is required to recalculate its public float whenever its registration statement is amended for purposes of updating the registration statement in accordance with Section 10(a)(3) of the Securities Act. This generally occurs each year when an issuer files its Annual Report on Form 10-K. If an issuer's public float is less than \$75 million at that time, the cap is then reimposed for subsequent sales.

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