MEMORANDUM

January 23, 1985

TO : Professional Staff
Division of Corporation Finance

FROM : Catherine C. McCoy CCMcCoy
Associate Director - Legal
Division of Corporation Finance

RE : Rule 415 and Related Issues

Rule 415 Issues

In recent months, a number of interpretive and policy issues involving Rule 415 have been brought to my attention. It is important that I be kept informed of such matters, and that the staff administer the Rule uniformly. Any registration statement which is selected for review should be examined for consideration of whether the offering will be either continuous or delayed, therefore requiring compliance with Rule 415, and if so, whether the Rule is in fact available for the particular offering. If the offering does not fit within any of the ten categories specified in Rule 415(a)(1), it may not be made on a continuous or delayed basis. The Rule should be interpreted strictly in order to assure that our administration of it reflects the Commission's concerns about disclosure and due diligence, expressed in the final adopting release (33-6499, November 17, 1983).

Any questions regarding the applicability or interpretation of Rule 415 should be directed to Bill Morley, Mauri Osheroff or me. Some examples of current Rule 415 issues which the staff should be aware of and bring to our attention are the following:

1. The Office of the Chief Counsel has received many questions, both from staff members and outsiders, about the distinction between primary and secondary offerings. It is important to identify whether a filing is intended to cover a primary or a secondary offering (or both), and whether a purported secondary offering is really a primary offering, i.e. the selling shareholders are actually underwriters selling on behalf of an issuer. In a situation not involving Rule 415 or Form S-3, the question of underwriter status may be resolved by additional disclosure and by an acknowledgment of the seller's prospectus delivery requirements. However, the distinction is particularly crucial for Rule 415 or Form S-3 filings because if the offering is deemed to be on behalf of the issuer, the Rule and Form in some cases will be unavailable. Specifically:

a. Many companies can meet transaction requirement B.3. of Form S-3 for a secondary offering, but would be unable to

use B.1. for a primary offering, since the latter imposes the "float" test.

b. Paragraph (a)(1)(i) of Rule 415 is available for secondary offerings, but primary offerings must meet the requirements of one of the other nine sections.

c. Many secondary offerings are equity at the market offerings. If such an offering is adjudged a primary one, it must meet the stringent requirements of Rule 415(a)(4), including eligibility for Forms S-3 or F-3.

Accordingly, the staff should pay close attention to the primary/secondary distinction in order not to erode the requirements of Form S-3 and Rule 415, which are designed to be stricter for primary offerings. The question of whether an offering styled a secondary one is really on behalf of the issuer is a difficult factual one, not merely a question of who receives the proceeds. Consideration should be given to how long the selling shareholders have held the shares, the circumstances under which they received them, their relationship to the issuer, the amount of shares involved, whether the sellers are in the business of underwriting securities; and finally, whether under all the circumstances it appears that the seller is acting as a conduit for the issuer.

One exception to the strict insistence on the primary/secondary distinction has been in the area of debt-equity swaps. While these transactions could be analyzed as offerings by underwriters on behalf of issuers, for policy reasons (related to the tax treatment of the transactions) it was decided that the B.3. transaction requirement of Form S-3 would be deemed available. However, it is not the policy of this Division to extend this position to any other type of transaction.

It should be noted that Rule 415 excludes from the concept of secondary offerings sales by parents or subsidiaries of the issuer. Form S-3 does not specifically so state; however, as a practical matter parents and most subsidiaries of an issuer would have enough of an identity of interest with the issuer so as not to be able to make "secondary" offerings of the issuer's securities. Aside from parents and subsidiaries, affiliates of issuers are not necessarily treated as being the alter egos of the issuers. Under appropriate circumstances, affiliates may make offerings which are deemed to be genuine secondaries.

In connection with the discussion of secondary offerings, the staff is frequently asked how registration statements for secondary offerings should reflect the addition or substitution of selling shareholders. Normally, absent circumstances indicating that the change is material, it may be reflected by the filing of a Rule 424(c) prospectus with a sticker describing the change and setting forth the information required by Item 507 of Regulation S-K. (Of course, the change should not involve increasing the number of shares or including shares from a transaction other than the one to which the original filing related.)

Note that the ability to reflect changes in selling shareholders by Rule 424(c) sticker does not permit the names of known selling shareholders to be omitted from the original filing.

2. We are frequently asked about situations in which registration statements are filed for secondary offerings, even though the securities are not yet issued because the primary sale has not yet taken place. Both policy considerations and form requirements should be considered. When the primary sale is to be made in reliance upon the 4(2) exemption, having a registration statement for resale on file before the private offering takes place would appear to cast doubt upon the validity of the exemption because distribution is clearly contemplated. In addition, when the registration statement is on Form S-3, the shares must be "outstanding" at the time of filing in order to be in compliance with transaction requirement B.3. (This requirement is not applicable to the S-3 prospectus that is filed with a Form S-8 for resale of securities acquired in an employee benefit plan.) Finally, the registration of a secondary offering under such circumstances may suggest doubt as to whether it is a genuine secondary, as discussed above.

3. Among the many innovative plans of financing seen today are those involving periodic adjustments of interest or dividend rates, rollovers of securities, and plans to buy back and remarket securities, sometimes coupled with "puts" or guarantees. Filings involving such plans require an analysis of Section 5 and Rule 415 issues. Even after the original offering of the securities has terminated, the registrant may still be engaged in a continuous or delayed offering with respect to the future periodic issuance or modification of securities. If so, the staff must determine whether Rule 415 is available. These issues should be brought to my attention, Bill's or Mauri's, as soon as they arise.

4. When Rule 415 was adopted in final form, it was specifically made unavailable for "sham shelves," that is, registration statements filed under Rule 415 as delayed offerings for procedural convenience only. Registrants who had an underwriter and a selling syndicate lined up and were ready to proceed with the offering would check the Rule 415 box, even though the offering was not to be made on a continuous or delayed basis, so as to avoid having to file a pricing amendment. As explained in Section VI.B. of Release 33-6499, this is no longer permitted. If it appears that a firm commitment offering of some or all of the securities registered will be commencing immediately upon effectiveness, the registrant should be advised that Rule 415 is inapplicable at least with respect to those securities contemplated to be sold immediately. A pricing amendment and distribution information should be obtained.

5. Rule 415(a)(1)(vii) permits a delayed or continuous offering in the case of mortgage-related securities. Although the 1933 Act and the rules thereunder do not define mortgage-related securities, the 1934 Act was recently amended to provide such a definition in Section 3(a)(41). Because the term in Rule 415 was intended to have the same meaning as ultimately decided upon by Congress, a security meeting the definition in 3(a)(41) will also be deemed to be a mortgage-related security for purposes of Rule 415. In the case of a traditional mortgage-related security offering which does not fall within the

definition, consideration should be given to whether another section of Rule 415(a)(1) is available, for example, sections (ix) or (x). Both of these sections, unlike section (vii), are subject to the two-year limitation of Rule 415(a)(2). We believe that by permitting section (vii) to be available only for mortgage-related securities as defined by the recent legislation, but at the same time permitting other sections of Rule 415 to be available for other filings involving mortgages, we will be adhering to the Congressional policy of facilitating the marketability of mortgages. The staff should consult with us if there is any difficulty in determining whether any section of Rule 415 is available to a mortgage-related security filing which falls outside the 1934 Act definition.

6. Item 512(a) of Regulation S-K, which is applicable to Rule 415 offerings, sets forth three circumstances requiring a post-effective amendment: Section 10(a)(3) updating, fundamental changes, and changes to the plan of distribution. (Forms S-3 and S-8 may accomplish the first two of these by incorporation by reference from 1934 Act reports, if the reports contain the required information.) A Rule 424(c) supplement should not be used for these purposes. Our attention should be directed to instances of stickers being improperly used, for example to change the entire offering and plan of distribution.

7. Questions have arisen concerning Rule 415(a)(2), which states that Rule 415(a)(1)(viii) through (x) may be utilized only for securities registered in an amount reasonably expected to be offered and sold within two years from the initial effective date. The registrant must make a bona fide estimate of this amount at the time of the initial filing. However, if at the end of the two years unsold securities remain, the registration statement may continue to be used. There is no requirement that the unused securities be deregistered after two years are up.

Additional Matters

Because of the interaction between Rule 415 and Form S-3, the above discussion addressed the requirements of Form S-3 in the context of the primary/secondary distinction. The importance of compliance with form requirements should be stressed in a more general context. In addition to checking for Rule 415 compliance, branches should pay particular attention to whether 1933 Act filings are on the correct form, especially when on forms of limited availability such as S-2, S-3 or S-15. As set forth by Rule 401, a registration statement must meet the form requirements at the time it is first filed, and also at the time of any 10(a)(3) post-effective amendment. A registration statement on one form may be changed to any other form for which it is then eligible by pre- or post-effective amendment. Once a filing is declared effective, it is deemed to be on the proper form, so any questions regarding form usage should be raised in timely fashion. Questions in this area should be addressed to Mauri or Bill. Requests for waivers of form requirements, which are only granted under very limited circumstances, are handled by Mauri; no waivers may be granted by staff members other than Bill or Mauri.

Securities to be issued in connection with business combinations may be registered on a shelf filing pursuant to Rule 415(a)(1)(viii). While this

section does not limit the form used, it should be noted that not all forms are available for business combinations. In particular, Forms S-2 and S-3 are not available for business combinations of any kind - exchange offers, Rule 145(a) transactions, etc. General Instruction I to Form S-2 states that the Form may be used for offerings of securities "in any transaction other than an exchange offer for securities of another person;" this instruction is interpreted as prohibiting the use of the form not only for third party exchange offers but also for any other business combination, however structured. The "for cash" proviso in the primary offering transaction requirements for Form S-3 has a similar effect. (This position is expressed in Note 14 to Release No. 33-6534 (May 9, 1984), which proposes for comment a new business combinations form, Form S-4.) However, there is no objection to the use of Forms S-2 or S-3 for a secondary offering of shares which were originally received from the issuer in connection with a business combination, assuming it is a genuine secondary offering, as discussed above.

In connection with the examination for compliance with form requirements, the rules relating to incorporation by reference of documents into prospectuses, or delivery of documents with prospectuses, should be interpreted strictly. Rule 411 states that incorporation by reference into a prospectus (as distinct from the incorporation of exhibits to registration statements) is prohibited unless the form specifically permits it. Therefore, there should be no incorporation by reference into an S-1 prospectus, even if the additional documents would be furnished with the prospectus. Form S-2 requires the incorporation by reference of certain previously filed documents, but does not permit the incorporation of subsequently filed documents. Also, Form S-2 permits the furnishing of an annual report to shareholders to offerees in lieu of including certain information in the prospectus, but the annual report on Form 10-K may not be substituted for the annual report to shareholders. Form S-3 requires the incorporation by reference not only of previously filed but of subsequent reports, and most updating of S-3 filings is therefore accomplished by the filing of 1934 Act reports. However, changes to information required to be in the prospectus itself and not specifically permitted to be incorporated by reference, such as information relating to selling security holders or the plan of distribution, must be accomplished by a Rule 424(c) prospectus supplement or post-effective amendment, as appropriate; see the above discussion of the 512(a) undertakings.

Conclusion

I hope that the above examples will assist the branches in identifying potential problems and bringing them to our attention. In addition, if Rule 415 problems that have occurred in the past (such as legality opinions with inappropriate conditions regarding future events) are resurfacing, let us know.

Finally, once again, it is important that the staff notify Bill, Mauri or me of the items highlighted above, as well as any novel questions or developing trends involving Rule 415, at the earliest possible point in order for the Division to develop consistent approaches in this area. Of course, novel questions and significant trends should also continue to be brought to the attention of the appropriate Associate Director-Operations.