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July 3, 2007

SEC Proposes Amendments to Form S-3 and Form F-3

The SEC has proposed for public comment amendments to the eligibility requirements of registration statements on Form S-3 and Form F-3. These amendments are intended to allow additional companies to benefit from the more flexible and efficient access to the public securities markets afforded by Form S-3 and Form F-3 without compromising investor protection. Under the proposed amendments, companies could conduct primary securities offerings on Form S-3 and Form F-3 without regard to the size of their public float or the rating of debt they are offering, as long as they satisfy the other eligibility requirements 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 form instructions over a period of 12 calendar months. The proposals are subject to a 60-day comment period.

The ability to conduct primary offerings on Form S-3 and Form F-3 confers significant advantages on eligible companies. These Forms permit 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, which allows for automatic updating of the registration statement. Form S-3 and Form F-3 eligibility for primary offerings also enables companies to conduct primary offerings "off the shelf" 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.

Proposed Revisions to Form S-3

To use Form S-3, a company must meet the Form's eligibility requirements set forth under General Instruction I.A. to Form S-3, as well as at least one of the Form's transaction requirements set forth under General Instruction I.B. to Form S-3. The SEC has proposed a new transaction requirement, to be set forth in General Instruction I.B.6. to Form S-3 (the "Proposed Instruction"), that would allow companies with less than U.S.$75 million in public float to register primary offerings of their securities on Form S-3, even if their securities are not traded on a national securities exchange, provided that the following conditions are met:

- the registrant satisfies the other registrant eligibility requirements for the use of Form S-3;
- the registrant is not a "shell company" and has not been a "shell company" for at least 12 calendar months immediately preceding the filing of the registration statement on Form S-3; and

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- the registrant does not sell more than the equivalent of 20% of its public float in primary offerings under the Proposed Instruction over any period of 12 calendar months.

Form S-3 Registrant Eligibility Requirements

The registrant must satisfy all of the other registrant eligibility requirements for the use of Form S-3. These eligibility requirements, set forth in General Instruction I.A. of Form S-3, include, among other things, the requirement that the registrant (a) 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; and (b) have been subject to the requirements of Section 12 or 15(d) of the Exchange Act and have filed in a timely manner all material required to be filed pursuant to Section 13, 14 or 15(d) of the Exchange Act for at least 12 calendar months immediately preceding the filing of the registration statement on Form S-3.

Prohibition on Use of the Proposed Instruction by Shell Companies

To take advantage of the Proposed Instruction, a registrant must not be a "shell company" and must not have been a "shell company" for at least 12 calendar months immediately preceding the filing of the registration statement on Form S-3. "Shell company" is defined in Section 405 of the Securities Act 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 or cash and cash equivalents, or (3) assets consisting of any amount of cash and cash equivalents and nominal other assets.

While the SEC recognizes the use of "shell companies" for many legitimate business purposes, it is wary that these entities may give rise to disclosure abuses. Therefore, "shell companies" would continue to be prohibited from registering securities in primary offerings on Form S-3 unless they meet the $75 million float threshold of General Instruction I.B.1. of Form S-3. A former "shell company" that cannot meet the $75 million public float threshold but otherwise satisfies the registrant eligibility requirements of Form S-3, however, would become eligible under the Proposed Instruction to use Form S-3 to register primary offerings of its securities once the following conditions are met:

- 12 calendar months must have passed after the registrant ceased to be a "shell company";

- the registrant must 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 (such information is typically required to be included in a Form 8-K when a company ceases to be a "shell company"); and

- the registrant must have been timely in its Exchange Act reporting for 12 calendar months.

20% Limitation on Primary Offerings under the Proposed Instruction in a 12 Calendar Month Period

To take advantage of the Proposed Instruction, the registrant must not sell more than the equivalent of 20% of its public float in primary offerings under the Proposed Instruction over any

12 calendar month period (although a larger amount may be registered for offerings from time to time over a period longer than one year). The proposal contemplates a two-step process for the calculation of this 20% threshold in connection with any intended sale of securities under the Proposed Instruction.

Step One: Determination of Public Float Immediately Prior to the Intended Sale

"Public float," as set forth in Instruction I.B.1. of Form S-3, means the aggregate market value of the voting and non-voting common equity held by nonaffiliates of a registrant. The registrant must determine its public float immediately prior to the intended sale, computed by reference to the price at which its common equity was last sold, or the average of the bid and asked prices of its common equity, in the principal market for the common equity as of a date within 60 days prior to the date of sale.

This method of calculating the registrant's public float is designed to allow registrants 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 an intended sale, as opposed to the time of the initial filing of the registration statement, the amount of securities that a registrant is permitted to sell can continue to grow over time if the registrant's public float increases. 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 a registrant is permitted to sell at any given time may also decrease if the registrant's public float contracts. Note, however, that a contraction in a registrant's public float, such that the value of 20% of the public float decreases from the time the registration statement was initially filed, would not necessarily violate 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 primary offerings in the preceding period of 12 calendar months, does not exceed 20% of the registrant's public float calculated within 60 days of the sale, then the transaction would not violate the Proposed Instruction 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 public float.

Step Two: Aggregation of Primary Offering Sales over Previous 12 Calendar Months

The registrant must aggregate the gross sales price for all primary offerings of its debt and equity securities under the Proposed Instruction in the previous 12-month period, including the intended sale. The SEC has included debt securities in the calculation in order to avoid inadvertently encouraging issuances of debt securities over equity securities. Registrants who meet the requirements of the Proposed Instruction would be eligible to offer non-investment grade debt securities on Form S-3 in addition to the non-convertible investment grade debt securities allowed under the current instructions for Form S-3.

In the case of securities that are convertible into or exercisable for equity securities (such as convertible debt or warrants), the proposal would require registrants to calculate the amount of securities they may sell in any 12 calendar month period by reference to the aggregate market value of the underlying equity security instead of the market value of the derivative securities. The aggregate market value of the underlying equity securities would be based on the maximum

number of equity securities into which the derivative 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 (which must be the same as the date chosen for the calculation of the registrant's public float in Step One described above), multiplied by the same per share market price of the registrant's equity securities used for purposes of calculating its public float pursuant to Step One described above.

The SEC has devised the method of calculation of the 20% threshold based on the market value of the securities underlying any derivative securities in order to reduce the risk that convertible securities would be structured and offered in a manner designed to avoid the effectiveness of the 20% limitation. The 20% limit on sales is not intended to impact a holder's ability to convert or exercise derivative securities and only applies at the time the registrant sells the derivative securities rather than at the holder's later conversion or exercise of such securities.

Effect of the Fluctuations in Public Float

Form S-3 registrants who meet the $75 million public 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 public float falls below $75 million subsequent to the effective date of the Form S-3. The SEC believes it appropriate to provide companies registering on Form S-3 pursuant to the Proposed Instruction the same flexibility if their public 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. To provide this flexibility, the Proposed Instruction would lift the 20% restriction on additional sales in the event that the registrant's public float increases to $75 million or more subsequent to the effective date of their Form S-3.

As is currently the case 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, which is 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 the Proposed Instruction and would remain in place until the registrant's public float equaled or exceeded $75 million.

Proposed Revisions to Form F-3

Form F-3, which was designed to parallel Form S-3, is the equivalent short-form registration statement form available for use by "foreign private issuers" to register securities offerings under the Securities Act. "Foreign private issuer" is defined in Rule 405 under the Securities Act as any foreign issuer other than a foreign government except an issuer that meets the following conditions: (a) more than 50% of its outstanding securities are directly or indirectly owned of record by residents of the United States and (b) any of the following (1) the majority of the executive officers or directors are United States citizens or residents, (2) more than 50% of its assets are located in the United States, or (3) its business is administered principally in the United States.

Like Form S-3, Form F-3 is available to foreign private issuers that satisfy (a) the form's eligibility requirements, which are similar to Form S-3 and generally relate to a registrant's

reporting history under the Exchange Act, and (b) at least one of the form's transaction requirements. Form F-3 limits the ability of registrants to conduct primary offerings on the form unless their worldwide public float equals or exceeds $75 million.

In order to maintain the rough equivalency between Form S-3 and Form F-3, which have the same public float criteria for primary offering eligibility, the SEC has proposed amendments to Form F-3 that are comparable to the proposed changes to Form S-3. Specifically, the proposed transaction requirements, to be set forth in 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 that the following conditions are met:

- the registrant satisfies the other registrant eligibility requirements for the use of Form F-3;
- the registrant is not a "shell company" and has not been a "shell company" for at least 12 calendar months immediately preceding the filing of the registration statement on Form F-3; and
- the registrant does not sell more than the equivalent of 20% of its public float in primary offerings under General Instruction I.B.5. of Form F-3 over any period of 12 calendar months.

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This memorandum is not intended to provide legal advice with respect to any particular situation, and no legal or business decision should be based solely on its content. Questions concerning issues addressed in this memorandum should be directed to any member of the Paul Weiss Securities Group, including:

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