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Company Registration in its Historical Context: Evolution Not Revolution

Miriam R. Albert
Maurice A. Deane School of Law at Hofstra University

COMPANY REGISTRATION IN ITS HISTORICAL CONTEXT: EVOLUTION NOT REVOLUTION

MIRIAM R. ALBERT*

I. INTRODUCTION

In recent years, there has been renewed interest in, and discussion about, changing the current system for registering securities under the Securities Act of 1933[1] ("Securities Act"). Under the current transaction-based system, issuers must register each non-exempt public offering of securities.[2]

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* Assistant Professor of Legal and Ethical Studies, Fordham University Schools of Business; LLM, New York University, 1997; JD and MBA, Emory University, 1987; BA, Tufts University, 1984. The author would like to thank those who provided valuable assistance: Daniel Berick, Mark Conrad, Ken Davis and Donna Gitter.

1 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-aa (1997)).

2 Section 5 of the Securities Act strictly prohibits all selling efforts prior to the filing of a registration statement, absent an exemption. *See* 15 U.S.C. § 77(e) (1997). These prohibitions are:

> [I]mplemented by regulating the scope of all offers as well as sales of securities so long as there is sufficient use of interstate commerce unless there is an applicable exemption. The basic purpose of [the Securities Act] registration requirement, as well as section 5's prohibitions and limitations on permissible offers to sell securities, is to assure that the investor has adequate information upon which to base his or her investment decision.

THOMAS LEE HAZAN, THE LAW OF SECURITIES REGULATION 78 (3d ed. 1996).

In keeping with the securities laws' stated goals of investor protection, the SEC established a three-tiered system of registration and prospectus disclosures, depending on the issuer's reporting history and market following—i.e., depending on how much information is already available to the public about a particular issuer. *See infra* notes 52-55 and accompanying text.

Commentators have begun to reexamine the desirability of so-called "company registration,"[3] whereby an issuer's registration is deemed to include all reports subsequently filed under the Securities Exchange Act of 1934[4] ("Exchange Act"), with only the actual transaction-specific terms required to be disclosed for any new offering of securities.[5]

These three tiers are manifested in the various forms of registration statements, primarily Forms S-1, S-2 and S-3. Form S-1 is to be used primarily by first-time issuers and issuers with securities publicly held by only a limited number of shareholders. The general instructions to the form indicate that it is to be used by all registrants "for which no other form is authorized or prescribed." Form S-2 permits incorporation by reference and is available to all domestic registrants with a class of securities registered under the Exchange Act who have participated in the continuous disclosure system set up by the Exchange Act for at least 3 years. Form S-3 is available to issuers who have at least one year of Exchange Act filings and a minimum net capitalization of $75 million (by non-affiliates). Form S-3 issuers need only include transaction specific information on the proposed offering. *See* Forms S-1, S-2 and S-3, Securities Act, 2 Fed. Sec. L. Rep. (CCH) ¶ 7121 (Oct. 13, 1999) ("Form S-1"); ¶¶ 7141-46 (Apr. 7, 1999) ("Form S-2"); ¶¶ 7151-55 (Mar. 31, 1999) ("Form S-3") (setting out the requirements for each form). *See* HAZAN, *supra* note 2, at 121-22; *see also* Stephen J. Choi, *Company Registration: Toward a Status-Based Antifraud Regime*, 64 U. CHI. L. REV. 567, 569 n.6 (1997). According to Professor Choi:

> The Securities Act already partially takes into account the range in the efficiency of trading markets for different companies' securities. Based on the likelihood that a company trades in an efficient market, the SEC partitions companies seeking registration into three groups: those eligible for Form S-1, S-2, or S-3 registration . . . Companies that meet the S-3 qualifications receive the greatest presumption of efficient market status and may incorporate the largest amount of information by reference from their most recent Exchange Act filings into the Securities Act registration statement. S-2 companies [have] a lower presumption of efficient market status and consequently [are allowed] less incorporation by reference . . . S-1 companies carry no presumption of efficient market trading and are consequently denied the ability to incorporate by reference.

Id. at 578-79.

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> [T]he core idea in company registration is that eligible companies should be able to make offers and sales of securities without submitting to a costly transaction registration process. Prospectus content – and, indeed, the use of any recognizable "prospectus" — would be determined by marketing needs and the general antifraud obligation to make full and fair disclosure of material information, instead of by a predetermined formula prescribed in the instructions to the SEC-mandated form of prospectus. Once a company became eligible for company registration, it would register under the '34 Act and thereafter file periodic reports under it. Routine financings would be consummated without any further '33 Act registration, and any prospectus that was in fact prepared for marketing purposes would be shaped by marketing needs, plus, of course, the antifraud rules of the '34 Act.

John C. Coffee, *Re-Engineering Corporate Disclosure: The Coming Debate Over Company Registration*, 52 WASH. & LEE L. REV. 1143, 1155 (1995).

4 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-jj (1997)).

5 In 1995, the SEC established an Advisory Committee on the Capital Formation and Regulatory Processes ("SEC Advisory Committee"), charging it with reviewing forms and rules relating to capital-raising transactions, and with advising the SEC on "the informational needs of investors and the regulatory costs imposed on the U.S. securities markets." *See* Charter of the Securities and Exchange Commission Advisory Committee on the Capital Formation and Regulatory Processes (February 24,

Company registration is not a novel idea,[6] and is best understood in its historical context. This requires an examination of the purposes and administration of the Securities Act and the Exchange Act, both of which were enacted in, and for, a very different economic and technological environment.[7] The stated purpose of the Securities Act is "to provide full

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1995, renewed February 21, 1996) *at* http://www.sec.gov/news/studies/capform/capffull.txt (last visited Feb. 28, 2001). For a detailed discussion of the SEC Advisory Committee's recommendations, *see infra* notes 104-166 and accompanying text.

According to Professor John C. Coffee, a leading scholar in the field of company registration:

> Under the "company registration" model outlined in the Final Report of the Advisory Committee on the Capital Formation and Regulatory Processes, an eligible issuer would file a one-time registration statement covering all its outstanding securities. Once effective, this registration statement would apply to all the issuer's securities (including securities thereafter authorized and issued), and all future 1934 Act reports automatically would be incorporated by reference. Other than a nominal fee paid at the time of the initial filing, the issuer would incur registration fees on a "pay-as-you-go" basis, at the time of individual sales.
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> Formal prospectus delivery would be largely eliminated, as the confirmation of sale would incorporate by reference the contents of the statutory prospectus (except in certain special transactions). Issuers electing "company registration" would be required to adopt certain "disclosure enhancements" that sought to improve the quality of their 1934 Act filings, and a Form 8-K would be required at the time of major equity takedown to cover material developments since the time of the issuer's last Form 10-Q (as well as to provide transaction-specific disclosures).

John C. Coffee, *1933 Act Deregulation: A Guide for the Perplexed*, N.Y.L.J., Sept. 26, 1996, at 5.

6 According to one commentator, company registration is a concept "whose time has come and gone and how has come again." *See* Choi, *supra* note 2, at 648.

7 The growth of capital markets, coupled with the increased number of institutional investors and advances in technology have combined to change the investing environment. In the 1930s, the capital markets and their investors were much less sophisticated and thus the time frame to complete a public offering was significantly longer, often taking six months or more for an underwriter to market and sell an offering. *See* Michael McDonough, *Death in One Act: The Case for Company Registration*, 24 PEPP. L. REV. 563, 566 n.31 (1997); *see also* Roberta S. Karmel, *Is § 5 an Anachronism?*, N.Y.L.J., Dec. 21, 1995, at 3.

> After more than 50 years on the books, the registration provisions of the Securities Act of 1933 – at least insofar as they apply to securities offerings by companies reporting under the Securities Exchange Act of 1934 – have outlived their usefulness.
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> A partial demise of the act's registration provisions has become desirable – even urgent – at this time for two important reasons.
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> First, the SEC is squandering resources by continuing to review 1933 act filings of reporting companies. These resources could be more usefully devoted to the review of issuers' periodic 1934 act disclosures as well as a more complete review of first-time registrants.
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> Second, the markets have changed in two important ways. The proliferation of new types of securities and distribution techniques has put increasing pressure on the 1933 act list of "exempt securities" and "exempt transactions," while the developing internationalization of the securities markets has created tension between the regulated domestic market and the "unregulated" Eurodollar market.

Joseph McLaughlin, *1933 Act's Registration Provisions: Is Time Ripe for Repealing Them?*, NAT'L L.J., Aug. 18, 1986, at 44.

and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof, and for other purposes."[8] The stated purposed of the Exchange Act is "to provide for the regulation of securities exchanges and of over-the-counter markets operating in interstate and foreign commerce and through the mails, to prevent inequitable and unfair practices on such exchanges and markets, and for other purposes."[9]

Completely absent from these stated purposes is any mention of needlessly burdening issuers with duplicative and onerous disclosure obligations, or of holding underwriters and other gatekeepers to a standard of care that may be functionally impossible to satisfy.[10] Yet despite significant modifications to both Acts over time, these are some of the results of the current registration system.[11]

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[8] The Preamble to the Securities Act of 1933, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-aa (1997)). The Securities Act is primarily concerned with the issuance of securities and thus is "transaction-focused." The statute requires issuers to make transaction specific disclosures to the market and to potential investors. *See* Choi, *supra* note 2, at 567, 614.

[9] The Preamble to the Exchange Act of 1934, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-jj (1997)). The disclosure requirements of the Exchange Act are not tied to specific transactions, but are instead triggered by an issuer's status, in terms of its trading history and market capitalization and asset base. *See* Choi, *supra* note 2, at 567.

[10] According to the SEC Advisory Committee, the current registration scheme:

> [I]mposes indirect and direct costs. The indirect costs include uncertainty and delay arising from the possibility of SEC staff review (including the possibility of losing a market window), market overhangs, short-selling and related activities, and publicity constraints. Direct costs include legal, accounting, underwriting, printing and filing fees.

SEC ADVISORY COMMITTEE, FINAL REPORT OF ADVISORY COMMITTEE ON THE CAPITAL FORMATION AND REGULATORY PROCESSES, app. A (July 24, 1996), *available at* http://www.sec.gov/news/studies/capform/capffull.txt (last visited Feb. 28, 2001) (hereinafter SEC Advisory Committee Final Report).

[11] For more than fifty-five years, the SEC has administered two parallel disclosure systems: one for the registration of public offerings under the Securities Act of 1933 and the other for the periodic reporting requirements of the Securities Exchange Act of 1934. The parallel systems resulted in a great deal of duplicative filings and unnecessary paperwork. In 1982, the Securities and Exchange Commission adopted an integrated disclosure system for registration of securities under the 1933 Act. While some duplication remains, the institution of integrated disclosures has made great strides in easing the disclosure burden. The current system integrates and simplifies the disclosure requirements under the 1933 and 1934 securities acts. The Commission has explained that its goal in adopting the new system was "to revise or eliminate overlapping or unnecessary disclosure and dissemination requirements whenever possible, thereby reducing the burdens on registrants while at the same time ensuring that security holders, investors and the marketplace have been provided with meaningful, non-duplicative information upon which to base investment decisions."

HAZAN, *supra* note 2, at 119-20 (citations omitted).

Some practitioners and commentators question the utility and wisdom of additional modification to a system that was arguably designed for another era.[12] Perhaps the system should simply be abandoned as being obsolete and interfering with efficient capital formation, with no compensating increase in investor protection.[13]

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[12] Former Commissioner Steven Wallman, who chaired the SEC Advisory Committee, questioned whether the "current registration requirements erect unnecessary obstacles to capital formation without producing countervailing benefits for investors." *See* Steven M. H. Wallman, *The SEC and the Capital Formation Process*, 9 INSIGHTS 3 (May 1995).

> As the Securities Act of 1933 completes its sixty-third year of existence, its future is more uncertain than at any other time in its history. Although its core principles were once hailed as "a permanent and integral part of our legal system," the 1933 Act now merits such descriptions as "obsolete" and its dictates are addressed in terms of "erosion." Now, the innovative "company registration" disclosure model, recently embraced by the Securities and Exchange Commission's Advisory Committee on the Capital Formation and Regulatory Processes may very well signify the demise of the 1933 Act altogether.

McDonough, *supra* note 7, at 563.

> Adopted during the depths of the Great Depression, the '33 Act predates the rise of institutional investors, modern finance theory and the new trading patterns that have blurred the differences between the primary and secondary securities markets. Nonetheless, it is far from a statutory anachronism. Thus, the real issues are to what extent the '33 Act no longer works and how it should be reformed.

John C. Coffee, *Securities Law*, NAT'L L.J., Sept. 11, 1995, at B4.

> Fundamental reforms are hard to achieve in the area of securities regulation, but nowhere more so than in the 1933 act sector. Lacking the glamour and economic clout of 1934 act issues such as market structure and tender offer regulation, 1933 act reforms tend to be held up by a timid and tradition-bound SEC staff, an uninterested (or at best suspicious) Congress and a complaisant securities bar. What is needed now is a serious consideration of the costs and benefits of 1933 act registration to determine whether, as Prof. Homer Kripke has suggested, it is "obsolete thinking" to continue to assert that registration still serves an important public policy.

McLaughlin, *supra* note 7, at 44.

[13] Laws and regulations are enacted in a given time period, presumably in the hope that they will be able to serve their purpose over some period of time. But this may not prove to be the case:

> Statutory obsolescence is the fate of all legislation. At some point in the natural "life cycle" of any statute, courts tend to move from purposive statutory construction, focused on the actual legislative intent, to greater deference towards administrative expertise as they implicitly recognize that the original legislative intent no longer fits the contemporary institutional landscape. *Given that the federal securities laws were passed during the 1930s, they have now* entered the geriatric zone where their possible obsolescence must be considered. Some academics have already called for the SEC's elimination on precisely this basis.

Coffee, *supra* note 3, at 1144; *see also* McDonough, *supra* note 7, at 563 n.185.

> The time has come for fundamental change in the amount and methods of disclosure required from companies issuing securities in the United States . . . the Securities Act of 1933 is outmoded and should be replaced with legislation implementing, with some changes, the pilot company registration system proposed by the Commission's Advisory Committee. In the alternative, the Advisory Committee should recommend that the Commission request

The more popular view, however, is somewhat less drastic, focusing on how to work within the existing regulatory framework, through either continued incremental modification,[14] or by substituting in a new, streamlined approach to registration — a company registration system.[15]

Either additional modification or introduction of an entirely new system would require statutory amendments by Congress or the exercise by the Securities and Exchange Commission ("SEC") of its statutorily-granted rulemaking authority.[16] Despite the SEC's rulemaking power, regulatory

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> broadened exemptive authority from Congress in order to implement most of the provisions of company registration through administrative rulemaking.

Id. at 564-65.

[14] The SEC "appears to be administratively repealing some of the Securities Act of 1933's clearest prohibitions. Independently, Congress seems intent on 'deregulating' the Securities Act of 1933, in part by making prospectus delivery optional with the investor." Coffee, *supra* note 3, at 1144. Some commentators have proposed additional steps:

> Repeal the registration provisions of the 1933 act for all securities offerings by reporting companies; preserve Sec. 12(2) liability for issuers, officers, directors, underwriters, etc. (with due- diligence defenses as in the case of Sec. 11) to individuals who purchase securities from an issuer or control person on the basis of a false or misleading offering document (or where no document was required to be furnished, on the basis of the issuer's 1934 act reports); and preserve the SEC's ability on an administrative basis to take action in the event of any sale of a security on the basis of false or misleading disclosure....
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> ....
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> Lawyers who have mastered over the years the minutiae of the 1933 act exemptions and the SEC registration process might find it difficult to accept the proposal. This includes, of course, the private bar and the professional SEC staff. After all, no '"priesthood"' likes to give up its accustomed rituals. One can only hope that practitioners would in time come to acknowledge the public benefits of redirecting their talents to an improvement in the continuous disclosure system.

McLaughlin, *supra* note 7, at 44.

[15] The current regulatory system crafted during the era of the Great Depression does not fully and most efficiently meet the needs and realities of today's markets, which are increasingly complicated by modern financing techniques, technological advancements, globalization, and changes in investors profiles and demands. These developments bring into question whether all types of companies should be subject to the current Securities Act's transactional registration requirements each time they desire to raise capital in the public markets. After concluding that the current structure was imposing unnecessary costs, while not fully taking into account the needs of today's investors, the [Advisory] Committee determined to recommend a shift in the focus of the regulatory structure from the current transactional system to a company registration system that would reduce these costs while enhancing investor protection.

SEC Advisory Committee Final Report, *supra* note 10, at app. A.

[16] Since the Securities Act was first enacted, the SEC has had statutorily-granted power to "make, amend, and rescind such rules and regulations as may be necessary to carry out the provisions of [the Securities Act of 1933], including rules and regulations governing registration statements and prospectuses." 15 U.S.C. § 77s (1997).

revision, at least with respect to the implementation of any major changes to the existing federal securities regulation landscape, has traditionally followed a somewhat cyclical model.

First, there is discussion in the academic and professional literature, commenting on, criticizing or proposing changes to some facet of the existing regulatory system ("public debate"); then, either overlapping with or following this public debate, the SEC may informally float non-binding suggestions for changes, through presentations at conferences, or unofficial articles and publications written by SEC staff members ("agency debate").[17] Again, perhaps overlapping with the agency debate, the SEC may next issue a formal statement, such as a release, containing proposals to address, and even further shape the discourse, seeking comments on the statements ("agency proposal"). After renewed public debate, and taking into consideration, to varying extents, the comments made, the SEC then exercises its rulemaking power and formalizes the revisions into rules ("agency action").

Because of the cyclical nature of the model, as new rules are enacted and put into effect, courts may have an opportunity to interpret them or to pass on their constitutionality, and commentators and the private bar have an opportunity to evaluate the success of the new rules and any deficiencies or other issues arising therefrom, generating additional public debate. Thus, in the aftermath of the agency action, the cycle starts all over again ("next public debate").

The agency action portion of the model has become much easier for the SEC to accomplish in recent years. The SEC is now authorized by statute to go beyond rulemaking simply to carry out the provisions of securities laws.[18]

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17 The SEC is always careful to at least nominally distance itself from these unofficial contributions to the discourse by including a disclaimer in all articles written by its staff. For example, in her article, Linda C. Quinn, then director of the SEC's Division of Corporation Finance offered the following disclaimer: "The Securities and Exchange Commission, as a matter of policy, disclaims responsibility for any private publication or statement by any of its members or employees. The views expressed herein are those of Ms. Quinn and do not necessarily reflect the views of the SEC or its staff." Linda C. Quinn, *Reforming the Securities Act of 1933: A Conceptual Framework*, 10 INSIGHTS 25, 26 (Jan. 1996).

These disclaimers should not be taken as a commentary on the substance of the pieces. For example, despite this disclaimer, Ms. Quinn's article has been cited by commentators, and in fact is specifically referenced in the SEC's concept release, seeking comments on company registration. *See* Securities Act Concepts and Their Effects on Capital Formation, Securities Act Release No. 33-7314, 61 Fed. Reg. 40,044, 40,051 n.57 (July 31, 1996).

18 The SEC has been given general exemptive authority to:

> [C]onditionally or unconditionally, exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of [the

One useful area for exercise of the SEC's general exemptive authority would be to adopt company registration, shifting the focus of the regulatory process from registering transactions to registering companies.[19] Under company registration, seasoned issuers subject to and in compliance with the continuous disclosure requirements of the Exchange Act[20] could make offers and sales of securities without additional registration under the Securities Act.[21] Eligible issuers would file a company registration statement, disclosing plans to make offerings from time to time, generically registering the types of securities and offerings contemplated, incorporating all existing and future

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> Securities Act] or of any rule or regulation issued under [the Securities Act], to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.

15 U.S.C. §§ 77z-3, 78mm (1997).

[19] For a full discussion of the company registration proposal recommended by the SEC Advisory Committee, *see infra* notes 104-166 and accompanying text.

[20] Registration under the Exchange Act triggers participation in the periodic disclosure system, including filing of Form 10-K (annual report), Form 10-Q (quarterly report) and Form 8-K (current report to report certain specified material changes in the issuer's conditions or operations). *See* Forms 10-K, 10Q, 8Q, Exchange Act, 5 Fed Sec. L. Rep. (CCH) ¶ 31,102-07 ("Form 10-K"); ¶ 31,031-35 ("Form 10-Q"); ¶ 31,001-04 ("Form 8-K").

[21] The SEC Advisory Committee recommended, and the SEC proposed, the institution of a company registration system, through the following steps:

> *on a one-time basis, the issuer files a registration statement (deemed effective immediately) that includes information similar to that currently provided in an initial short-form shelf registration statement. This registration statement could then be used for all types of securities and all offerings (including those offered in furtherance of business acquisitions) and all offerings could be subject to Section 11 strict liability;
>
> *current and future Exchange Act reports are incorporated by reference into that registration statement;
>
> *around the time of the offering, transactional and updating disclosures are filed with the SEC, usually in a Form 8-K that is incorporated by reference into the registration statement and subject to Section 11 strict liability, but in certain cases, at the option of the issuer, through a prospectus supplement like those traditionally filed in shelf takedowns;
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> *other than a nominal fee paid at the initial filing, registration fees would be paid at the time of sale rather than prior to making any offers (the "pay as you go" feature);
>
> *issuers would be required to adopt some disclosure enhancements (and encouraged to adopt others) that seek to improve the quality and timeliness of disclosure provided to investors and the markets; and
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> *formal prospectuses would be required to be physically delivered only in non-routine transactions and, when so required to be delivered, they would have to be delivered in time to be considered in connection with the investment decision. In almost all instances, an issuer could incorporate by reference filed information into selling materials or the confirmation of sale to satisfy the legal obligation to deliver a prospectus (which, under the statute, must precede or accompany a confirmation of sale).

See Securities Act Concepts and Their Effects on Capital Formation, 61 Fed. Reg. at 40,044.

periodic reports. The registration form would be automatically updated by each Exchange Act filing.[22]

The idea behind company registration is that reporting companies have already given the market all of the material information necessary to support an informed investment decision, and such information is already reflected in the market price of the securities. Thus, there is no need for any additional registration of any particular transaction itself, since no further informational advantage would be gained.[23]

A company registration system, with all eligible issuers participating, would obviate much of the need for the complexities necessary to protect the paradigm of transactional registration, such as classifying securities as "restricted,"[24] determining what constitutes a "general solicitation"[25] and when offers are to be integrated.[26]

Agency action to adopt a company registration system is the next logical step in the progression from a transaction-based registration system to a company-based registration system. This progression includes the public debate and agency action that was the precursor of company registration[27] — the adoption of the integrated disclosure system for the primary offering and secondary trading markets[28] and the adoption of the shelf registration

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[22] *See* SEC ADVISORY COMMITTEE, THE CAPITAL FORMATION AND REGULATORY PROCESSES: TERM SHEET FOR PILOT COMPANY REGISTRATION SYSTEM 1 (July 24, 1996) *available at* http://www.sec.gov/news/studies/capform/capffull.txt (last visited Feb. 28, 2001) (hereinafter SEC Advisory Committee Term Sheet).

[23] *See* Donald C. Langevoort, *Theories, Assumptions, and Securities Regulation: Market Efficiency Revisited*, 140 U. PENN. L. REV. 851, 875 (1992).

[24] Securities acquired directly or indirectly from an issuer in a non-public offering, are considered to have the status of § 4(2) "restricted securities" and cannot be resold without registration or further exemption. *See* ALAN R. PALMITER, SECURITIES REGULATION 134 (Aspen Law & Business, 1998).

[25] Regulation D prohibits "general solicitations or general advertising" in a Rule 505 or 506 offering: this prohibition is designed to "ensure that the issuer (or its financial adviser) knows the investment sophistication and financial circumstances of all offerees. In effect, it mandates that suitability screening occur before any Regulation D solicitation – not as part of the solicitation." *Id.* at 133.

[26] *See* Wallman, *supra* note 12, at 3.

[27] Over the last thirty years, the [SEC] has begun to acknowledge the increasing pressures for change. Beginning with adoption of the integrated disclosure system in 1980, the Commission has made some headway toward combining the disclosure requirements of the 1933 Act and the Exchange Act of 1934 to arrive at a coordinated, non-duplicative, and less costly system of disclosure. Regulation S-K, adopted in 1982, itemized several areas of disclosure common to 1933 and 1934 Act filings in an attempt to synthesize information provided by companies subject to both Acts. Shelf registration emerged from the integrated disclosure system as a way for issuers to go to the market more efficiently and more often by relying on disclosures required under the 1934 Act.

McDonough, *supra* note 7, at 564.

[28] *See* Adoption of Integrated Disclosure System, Securities Act Release No. 33-6383, 47 Fed. Reg. 11,380, 11,384 (Mar. 16, 1982).

process.[29] This was followed by the penultimate step towards a company-based registration system, the universal shelf.[30]

Arguably, the entire federal securities regulatory system fits into the cyclical model. This Article, however, is limited to an exploration of the company registration proposal put forth by the SEC in July 1996 in its historical context. Part II of this Article is an application of the cyclical model to the adoption of the integrated disclosure system and the shelf registration process. Part III is an application of the cyclical model to the SEC's company registration proposal as a logical outflow of prior debates, including a discussion of possible issues left unresolved by or raised by the company registration proposal that may generate the next public debate, with a recommendation that the SEC adopt company registration.

II. ADOPTION OF THE INTEGRATED DISCLOSURE SYSTEM AND SHELF REGISTRATION PROCESS

A. *The Public Debate*

The public debate culminating in the adoption of the integrated disclosure system and shelf registration process stemmed at least in part from the separate nature of the Securities Act and the Exchange Act, and the inefficiencies resulting therefrom.[31] The Securities Act is a system of transaction-based disclosure, with the timing of disclosures linked to an issuer's sale of securities.[32] The Exchange Act superimposes a separate

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[29] *See* Shelf Registration, Securities Act Release No. 33-6499, 48 Fed. Reg. 52,889, 52,890 (Nov. 23, 1983). Shelf registration is governed by Rule 415; *see also* 17 CFR § 230.415 (1999). Under Rule 415(a)(1)(x), an issuer can register securities "to be offered and sold on a continuous or delayed basis" if the issuer qualifies for Form S-3 or Form F-3. *See id.*

[30] *See* Simplification of Registration Procedures for Primary Securities Offerings, Securities Act Release No. 33-6964, 57 Fed. Reg. 48,970, 48,974 (Oct. 29, 1992). Under the universal shelf:

> [E]ligible issuers could register debt, equity or other securities on a single shelf registration statement without having to specify the amount of each class of securities to be offered. As a practical matter, this minimized the market penalty that some issuers had incurred by filing an equity shelf registration statement (because the announcement of an equity offering usually leads to a decline in the issuer's stock market price).

Coffee, *supra* note 5, at 5.

[31] *See* HAZAN, *supra* note 2, at 119-20.

[32] Section 5 of the Securities Act regulated disclosure in a public offering; these rules are commonly referred to as the "gun jumping" rules. No security may be offered, unless a registration statement has been filed with the SEC no prospectus may be disseminated unless it contains the statutorily-specified information and no security may be sold or delivered unless the registration statement has been declared effective, and all investors have received a formal prospectus. *See* 15 U.S.C. § 77(e) (1997); *see also* Palmiter, *supra* note 24, at 100-01; Choi, *supra* note 2, at 605-06.

regime of company-specific disclosure, creating a system of continuous, periodic disclosure, which, if complied with fully and in a timely manner, substantially reduces the need for transaction-specific disclosure when an issuer later seeks to sell its securities.[33] The Securities Act and the Exchange Act historically were administered essentially independently; the two statutes required similar and sometimes duplicative information, with inconsistent presentation requirements.[34] As a result of this overlapping registration system, even seasoned issuers making timely disclosures to the market through the continuous disclosure system as required by the Exchange Act, and thereby fully informing the market of information necessary to make an investment decision, must also register public offerings of their securities under the Securities Act.[35]

The first significant attempt at legislative reform to address this overlap came in the form of agency debate, with an SEC-appointed committee, including Professor Louis Loss, and an industry-appointed committee, both charged with examining the provisions of the Securities Act and the Exchange Act. Hearings before the House Commerce Committee in 1941 on the committees' recommendations to Congress yielded no significant changes in the law. The concept of legislative reform resurfaced in the late 1950s, this time resulting in the introduction of several bills, but again, Congress did not take action.[36] Then Congress enacted the Securities Act Amendments of 1964, significantly revising the Exchange Act to bring over-the-counter issuers within its registration requirements, and arguably

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33 For an overview of the Securities Act and the Exchange Act, *see* McDonough, *supra* note 7, at 565-83.

> [I]n the case of reporting companies, the] 10-K and other 1934 act reports are the most important SEC-mandated disclosure documents, providing information to investors either directly (often by electronic means) or through the medium of securities analysts. This is the result intended by the SEC, of course, when as part of the "integrated disclosure system" it permitted many issuers to incorporate their 1934 act reports into 1933 act prospectuses. Given the success of the system and the parallel disclosure requirements under the two acts, it is hard to see how investors benefit – from a disclosure point of view – by 1933 act registration of a particular securities offering.

McLaughlin, *supra* note 7, at 44.

34 *See* Edward F. Greene, *Integration of the Securities Act and the Exchange Act: A Case Study of Regulation in the Division of Corporate Finance of the United States Securities and Exchange Commission*, 3 J. COMP. CORP. L. & SEC. REG. 75, 76 (1981).

35 "For decades, the '33 and '34 Acts were administered independently and seemingly almost in oblivion of each other. Not only was duplicative information required under each, but the manner of its required presentation was different and terms used in common by both Acts were defined differently by each." Coffee, *supra* note 3, at 1158.

36 *See* Louis Loss, *The American Law Institute's Federal Securities Code Project*, 25 BUS. LAW. 27, 29 (1969); *see also* Coffee, *supra* note 3, at 1145.

satisfying whatever desire Congress had then to overhaul the securities laws.[37]

However, participants in the public debate were far from satisfied with this new state of affairs; increasing the coverage of the Exchange Act exacerbated the complications resulting from the lack of integration between the Securities Act and the Exchange Act. The public debate on integration began in earnest with the 1966 publication of Milton Cohen's widely respected article *"Truth in Securities" Revisited*, in which he proposed a model for updating the federal securities laws.[38] Cohen's thesis was that securities regulation would look very different if the Exchange Act had been enacted first, or if the two Acts had been enacted as a single, comprehensive statute. Cohen proposed a fully integrated continuous disclosure system, under which the issuer would be required to disclose only material information not previously disclosed.[39]

A concurrent component of the public debate, proposing much the same solution, but aimed more directly at generating some form of agency action, was the American Law Institute's *Federal Securities Code* ("ALI Code"), an attempt to re-codify all six federal securities statutes into a single comprehensive code.[40] This project was inspired in part by the Cohen article

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37 *See* 78 Stat. 565 (codified as amended in scattered sections of 15 U.S.C.).

38 *See* Milton Cohen, *"Truth in Securities" Revisited*, 79 HARV. L. REV. 1340 (1966).

39 *Id.* at 1341, 1406-08; *see also* Coffee, *supra* note 3, at 1144-45. According to Professor Choi:

> In assessing the two regimes, Cohen recognized that disclosures pursuant to a public offering under the Securities Act consist of information that all investors require prior to making an investment decision, including not only those investors purchasing from the offering, but also those trading in the secondary market. From this observation, Cohen called into question the need for mandatory disclosures directed towards parties of any particular transaction and argued for the reform of the securities regime toward one, unified company-based information disclosure scheme.

Choi, *supra* note 2, at 567.

40 *See* The Securities Act of 1933, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-aa (1997)); The Securities Act of 1934, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-jj (1997)); The Public Utility Holding Company Act of 1935, 49 Stat. 803 (codified as amended at 15 U.S.C. §§ 79 1997)); The Trust Indenture Act of 1939, 53 Stat. 1149 (codified as amended at 15 U.S.C. §§ 77aaa et seq. (1997)); The Investment Company Act of 1940, 54 Stat. 847 (codified as U.S.C. §§ 80a-1 et seq. (1997)); The Investment Advisers Act of 1940, 54 Stat. 847 (codified as amended 15 U.S.C. §§ 80b-1 et seq. (1997)).

The goal of the ALI Code was:

> [N]ot only to achieve a unifying integration of these separate statutes, addressed at different times to closely related problems, but also to point the way toward their improvement, clarifying their obscurities, eliminating inconsistencies, articulating important norms developed in interpretive judgments and, within the limits of the basic legislative policy, proposing improvements that informed opinion favors and seems ready to support.

1 ALI, FEDERAL SECURITIES CODE at vii-viii (1980).

and championed by Professor Loss.[41]

The ALI Code is a comprehensive model of an integrated securities law, building disclosure around registering companies, not registering transactions — in other words, company registration. Thus, each new securities issue would not require a separate registration statement—all the information, including all periodic disclosure documents filed under the Exchange Act, would already be in the issuer's file. The information contained in the company registration statement, updated to reflect material changes, would be the main source of information to be incorporated into the "offering statement" that registered the specific securities offered, as well as the "prospectus," to be delivered to purchasers upon confirmation of sale and delivery.[42]

Drafting of the ALI Code began in the Fall of 1969 and was completed in 1978.[43] This time span is notable both for its duration and for its varying regulatory and political climate. While the project started out during a period favorable to federal regulation, over the life of the project, the regulatory climate shifted towards deregulation: the Supreme Court began limiting federal involvement in securities laws and the membership of the SEC shifted towards more laissez-faire economists.[44] By the time the ALI Code

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According to Professor Loss, the ALI Code had three principal aims: (i) simplification of an "inevitably complex body of law in the light of almost a half-century of administration and litigation;" (2) elimination of duplicate registration, to the extent possible; and (3) reexamination of the entire scheme of investor protection in the hopes of increasing its efficiency. *See id.* at xix.

[41] *See* Choi, *supra* note 2, at 568. Professor Loss' approach was not to criticize the SEC in its administration of the various securities laws, but instead to acknowledge that "because of the failure to recognize by appropriate legislation that, although the registration and prospectus machinery was central to disclosure in 1933, other disclosure devices have since been developed that are even more effective." *See* Loss *supra* note 36, at 28-30.

[42] *See* Gerald S. Backman & Stephen E. Kim, *A Cure For Securities Act Metaphysics: Integrated Registration*, 9 INSIGHTS 18, 20 (May 1995).

[43] Professor Loss had been quoted as saying that the securities laws should be codified, even if it took twenty years; he later clarified that, saying the remark:

> [W]as misinterpreted by some people as a prediction that codification would take twenty years. Now, maybe it will— I hope it won't— but certainly I don't predict it will, and certainly it should not. The point is, though, that in any event it's going to take longer than administrative reform, so in that sense alone there is no inconsistency.

Loss, *supra* note 36, at 32.

Professor Loss showed unfortunate prescience in his description of the time commitment necessary for a project of this magnitude: "[A]s in any codification effort, constant attention will also have to be paid to the extent to which we want to draft an ideal code and the extent to which we shall have to be practical. *I don't think any of us who would be doing the work would be interested in devoting four or five years to an academic exercise.*" *Id.* at 37.

[44] For a discussion of the changes in regulatory climate, *see* Robert W. Hamilton, *The State of State Corporation Law: 1986*, 11 DEL. J. CORP. L. 3, 18-19 (1986).

was finally finished, despite formal approval by the ALI and the SEC,[45] and the support of the American Bar Association and much of the private bar, it was never enacted into law.[46]

B. *The Agency Debate and Proposals*

Despite the lack of Congressional action on statutory integration, either through the ALI Code or otherwise, during the 1980s, the SEC, after proposing ideas for comment, exercised its rulemaking authority to implement many of the most popular ideas in Cohen's article and in the ALI Code.[47] The SEC attempted to effectively integrate the disclosure system by equalizing the requirements under the Securities Act and the Exchange Act,[48] such as incorporation by reference[49] and shelf registration for certain seasoned issuers,[50] but stopped short of proposing a company registration system.[51]

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[45] "Despite completion of the Code in 1980 and Commission approval, Congress was reluctant to dismantle the venerable 1933 and 1934 Acts with an untried system, and quietly forgot the Code in the absence of a strong lobby outside the Commission itself." McDonough, *supra* note 7, at 587.

[46] Congress declined to act, thereby choosing to retain the dual transaction and status based framework. *See* Choi, *supra* note 2, at 569. "When the ALI's Federal Securities Code was presented to Congress in 1980, Congress essentially yawned and declined to act. Unfortunately, 'good government' reform does not excite powerful constituencies nor generate the level of emotion necessary to stir a lethargic Congress into action." Coffee, *supra* note 3, at 1145-46.

> While this code ultimately was not enacted into law by Congress, it has been cited, I believe, more frequently than any other unadopted legislative proposal in this country's history, and has served as the inspiration for a number of law reforms at the SEC. Most recently, when Commissioner Steven M.H. Wallman sought a new approach to the SEC's mandatory disclosure system in 1997, he drew on the Federal Securities Code's company registration model.

Joel Seligman, *He Wrote the Book on Securities Regulation*, NAT'L L.J., Dec. 29, 1997/Jan. 5, 1998, at A15.

[47] "The SEC also looked into the possibility of moving toward a company registration system immediately after Cohen's article was published during the 1960's, an investigation that culminated in the Wheat Report." Choi, *supra* note 2, at 568 n.9.

[48] "Based upon the conclusions of the Wheat Report, as well as the recommendations of the Commission's Advisory Committee on Corporate Disclosure published in 1977, the Commission moved to integration of the disclosure requirements of the Securities Act and the Exchange Act." SEC Advisory Committee Final Report, *supra* note 10, app. B.

[49] Seasoned issuers are permitted, under certain circumstances, to incorporate into a registration statement filed under the Securities Act various other filings, such as Forms 10-K, 10-Q and 8-K. *See supra* note 20.

[50] *See supra* note 29 and accompanying text.

[51] "The Commission's basic strategy was to make the periodic reports filed under the '34 Act contain disclosure equivalent to that which would be in a '33 Act prospectus, and then to allow certain widely followed companies to incorporate by reference the information from their periodic reports into their prospectuses at the time they made a subsequent public offering." Coffee, *supra* note 3, at 1158; *see*

While the SEC developed the integrated disclosure system, it considered what information was material to investment decisions in public offerings of securities. The SEC concluded that full integration required that whatever was material for transactional reporting under the Securities Act was also material for periodic reporting under the Exchange Act. Integration, therefore, meant that the substantive requirements for the two Acts should be comparable.[52]

The SEC also considered under what circumstances such material information should be disseminated to security holders, investors and the marketplace, and determined that the dissemination of information should depend on the degree to whith the market has already been informed.[53] The SEC tacitly accepted the basic idea of the "efficient market hypothesis," that financial analysts and market participants absorb information so the market reaches the "correct" price; an adequately informed market does not need duplicative information to correctly price outstanding securities.[54] With these considerations in mind, the SEC proposed the integrated disclosure system with its three-tiered registration structure,[55] permitting increasing amounts of information to be incorporated by reference from previous filings, and the shelf registration system.[56]

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also Donald C. Langevoort, *Colloquium: Rule 10b-5 as an Adaptive Organism*, 61 FORDHAM L. REV. 7, 16 n.50 (1993); Loss, *supra* note 36, at 31.

[52] *See* Proposed Comprehensive Revision to System for Registration of Securities Offerings, Release No. 33-6235, 45 Fed. Reg. 63,693, 63,696 (Sept. 25, 1980); *see also* Adoption of Integrated Disclosure System, Securities Release No. 33-6383, 47 Fed. Reg. 11,380, 11,388 (Mar. 16, 1982); Backman & Kim *supra* note 42, at 19.

[53] *See* Proposed Comprehensive Revision to System for Registration of Securities Offerings, 45 Fed. Reg. 63,693, 63,695 (Proposed Sept. 25, 1980); *see also* Backman & Kim *supra* note 42, at 19.

[54] *See* Langevoort, *supra* note 23. According to the SEC:

> The dissemination requirements have been developed, in part, on the premise that information regularly furnished to the marketplace through formal Exchange Act periodic reports and informal corporate communications may be reflected in the price of the outstanding securities and thus need not always be reiterated in a prospectus in the context of a distribution.

Adoption of Integrated Disclosure System, 47 Fed. Reg. at 11,381.

[55] *See* text *supra* note 2.

> After the securities laws were expanded to give the SEC jurisdiction to mandate annual and periodic, as well as transactional, disclosure for all public companies, the dichotomy between transactional and annual financial reporting came under criticism and integration of the Securities Act and Exchange Act was advocated. In response, the SEC developed its integrated disclosure system whereby annual and periodic reports filed pursuant to the Exchange Act by seasoned issuers could be incorporated by reference in offering documents filed pursuant to the Securities Act. Further, securities could be registered and put on the shelf for future offering when advantageous capital windows were opened.

Karmel, *supra* note 7, at 3.

[56] *See* Adoption of Integrated Disclosure System, 47 Fed. Reg. at 11,388; *see also* text *supra* note 2.

The SEC had long resisted the idea of shelf registration of securities in excess of amounts that the issuer intended to offer,[57] nominally because of the statutory problem in the language of § 6(a) of the Securities Act,[58] and actually out of a concern that advance registration would lead to prospective investors relying on stale information.[59] Integrated disclosure would solve this by incorporating subsequently filed Exchange Act filings, thereby keeping the prospectuses current.[60] The SEC began to back away from a rigid interpretation of § 6(a), and by the early 1960s it became clear that certain types of offerings could be made by shelf registrations statements.[61]

Section 7 controls the content of registration statements, and authorizes the SEC to allow certain omissions in registration statements in respect of any class of issuers or securities if it finds that that the requirement of the omitted information "is inapplicable to such class and that disclosure fully adequate for the protection of investors is otherwise required to be included within the registration statement." 15 U.S.C. § 77g (1997).

Section 10 controls the content of prospectuses, and § 10(a)(4) allowing the SEC to omit any information not "necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 77j (1981); *see also* Backman and Kim, *supra* note 42, at 18-19.

57 An amendment to the Securities Act modifying § 6(a) to permit shelf registration was opposed by the SEC, and never enacted. *See* H.R. 4344, 77th Cong. (1941); S. 3985 76th Cong. (1940).

58 Section 6(a) provides that a registration statement "shall be deemed effective only as to securities specified therein as proposed to be offered." The SEC traditionally interpreted this provision to mean that registering more securities than the issuer presently intended to offer would be misleading. Rule 415 now permits issuers to register an amount of securities that "is reasonably expected to be offered and sold within two years from the initial effective date of the registration," not to exceed ten percent of the issuer's voting stock. *See* Rule 415(a)(2), 17 C.F.R. § 230.415(a)(2) (1999); Rule 415(a)(4)(ii), 17 C.F.R. § 230.415(a)(4)(ii) (1999); *see also* Scott Hodes, *Shelf Registration: The Dilemma of the Securities and Exchange Commission*, 49 VA. L. REV. 1106, 1108-15 (1963).

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> For decades, the SEC had resisted the shelf registration of securities in excess of the amount that the issuer then intended to offer, for fear that advance registration would mean stale prospectuses. . . . In 1983, the Commission accepted the arguments for shelf registration and broadened Rule 415 to permit an issuer to register up to approximately ten percent of its voting stock for sale in delayed "at the market" offerings. However, the issuer was required to certify that it "reasonably expected to . . . [offer and sell the amount so registered] within two years from the initial effective date of the registration.

Coffee, *supra* note 5, at 1158-59; *see also* McDonough, *supra* note 7, at 590.

60 *See* Coffee, *supra* note 3, at 1158.

61 *See* CHARLES J. JOHNSON JR., CORPORATE FINANCE AND THE SECURITIES LAWS 381 (Prentice Hall Law & Business 1990).

Under Rule 415, registrants may register securities:

> [I]n an amount which, at the time the registration statement becomes effective, is reasonably expected to be offered and sold within two years from the initial effective date of the registration . . . where voting stock is registered, the amount of securities registered for such purposes must not exceed 10 percent of the aggregate market value of the registrant's outstanding voting stock held by non-affiliates of the registrant [calculated as of a date within 60 days prior to the date of the filing].

17 C.F.R. § 230.415(2) (1999).

The adoption of shelf registration followed the cyclical model of regulatory development; the agency action by the SEC culminating in its adoption of Rule 415, involved extensive public and agency debate and a number of agency proposals.[62] In response to the public debate on its proposals, the SEC adopted shelf registration under Rule 415 on a temporary basis, in order to afford continued consideration.[63] The SEC proposed monitoring the operations of the Rule, while holding public hearings on issues such as investor protection under the Securities Act, capital raising by corporate issuers through shelf registration and due diligence concerns.[64] The SEC then extended Rule 415's effectiveness.[65]

Not all of the SEC Commissioners were enthusiastic about the possibility of shelf registrations. Commissioner Thomas, in her dissent to

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[62] First, the SEC proposed the rescission of the Guides for the Preparation and Filing of Registration Statements and Reports, except for Guides for disclosure by issuers in a particular industry. Included in the proposal was the rescission of Guide 4, which contained the instances in which shelf registration was contemplated. The SEC published proposed Rule 462A (Delayed or Continuous Offering and Sale of Securities) for comment, a comprehensive position with respect to shelf registration statements. *See* Proposed Revision of Regulation S-K and Guides for the Preparation and Filing of Registration Statements and Reports, Securities Release No. 33-6276, 46 Fed. Reg. 78, 87 (Jan. 2, 1981).

Proposed Rule 462A was largely ignored, perhaps because it was essentially buried in a lengthy release proposing for comment, among other things, the reorganization of Regulation S-K and the elimination or incorporation into Regulation S-K or Regulation C of all almost all of the guides. Some of the public commenters on Rule 462A expressed concern that the rule had not received sufficient attention because of its placement in the lengthy release; they recommended that the rule be republished in a separate release. *See* JOHNSON, *supra* note 61, at 397; *see also* Delayed or Continuous Offering and Sale of Securities, Securities Release No. 33-6334, 46 Fed. Reg. 42,001, 42,003 (Aug. 6, 1981).

The SEC then reproposed Rule 462A in a separate release, Securities Release No. 33-6334, 48 Fed. Reg. 52,889 (Aug. 6, 1981), which received much attention, mostly from panicked investment banks, fearing that the rule would undermine or impair the "traditional manner in which securities had been distributed to the public— fixed price offerings through underwriting syndicates." *See* JOHNSON, *supra* note 61, at 397.

[63] *See* McDonough, *supra* note 7, at 590.

[64] *See* Examination of the Registration of Securities to be Offered and Sold on a Delayed or Continuous Basis in the Future, Securities Release No. 33-6391, 47 Fed. Reg. 11,701,11,702-03 (Mar. 18, 1982).

[65] This action was taken in view of:

> [T]he number of commentators who believe that insufficient time has elapsed since the Rule became effective to assess its full impact and in light of the market conditions which have prevailed during this period . . . it is necessary to extend the period during which Rule 415 is effective to December 31, 1983 in order to obtain sufficient experience upon which to base [the SEC's] final determination of the Rule. The Commission believes that an additional twelve month period is appropriate, because it would provide a greater opportunity to study the operation and impact of Rule 415 through what may be a full financial cycle.

Delayed or Continuous Offering and Sale of Securities, Securities Release No. 33-6423, 47 Fed. Reg. 39,790, 39,799 (Sept. 10, 1982).

the SEC's approval on shelf registration, argued that Rule 415 as proposed posed risks to the capital markets and to the disclosure system, and "incurring these risks is antithetical to the statutory duty of the Commission to protect investors and to maintain the integrity of our capital markets."[66] With respect to the capital markets, she was of the opinion that the Rule, especially when applied to equity offerings, would jeopardize "the liquidity and stability of our primary and secondary securities markets by encouraging greater concentrations of underwriters, market-makers, and other financial intermediaries and by discouraging individual investor participation in the capital markets thereby furthering the trend towards institutionalization of securities holders."[67] She believed that the short turn-around time permitted by a shelf registration might impede the formation of traditional underwriting syndicates, and instead encourage smaller syndicates, resulting in the elimination of most small and regional broker-dealers from major underwritings.[68]

With respect to the disclosure system, Commissioner Thomas argued that further accelerating the registration process through shelf registration might reduce the quality and timeliness of disclosure available to investors.[69] Because of the accelerated timing of registrations under the Rule, the underwriters would not have sufficient time to perform adequate due diligence, thereby undercutting investors' ability "to rely upon the underwriters' obligation to interpose itself between the issuer and investor and to investigate the disclosures contained in the prospectus."[70]

To alleviate these concerns, Commissioner Thomas suggested limiting the principal application of Rule 415 to debt offerings, prohibiting its general use for primary equity offerings, and imposing a "notice period" of two business days for debt issuances not registered on Form S-3.[71]

Commissioner Thomas and other critics of the proposed shelf registration feared that it would limit the amount of due diligence that underwriters could (or would) undertake. But in the years since the adoption of the shelf registration system, while it is clear that advance due diligence for shelf offerings has declined as a result of their truncated timetables, there have been no "memorable scandals" resulting therefrom.[72]

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66 *See id.* at 39803 (Commissioner Thomas dissent).

67 *Id.*

68 *See id.* at 39809.

69 *See id.* at 39806.

70 *See id.* at 39807.

71 *See id.* at 39804.

72 *See* Coffee, *supra* note 3, at 1169.

Commissioner Thomas' concerns were not unfounded and many resurfaced during the recent discourse on company registration. A company registration system might alleviate some of these concerns, specifically by eliminating the two-year and ten percent limitations of Rule 415, allowing registration statements to be "evergreen."[73]

C. *The Agency Action*

In addition to the adoption of shelf registration, the SEC in 1982 also adopted the integrated disclosure system in an effort to address the duplicative disclosure under the Securities Act and Exchange Act, including the expansion and revision of Regulation S-K, which set out disclosure standards for both Acts.[74] To avoid duplication, the SEC also adopted the three-tiered registration system[75] to allow progressively more information to be incorporated by reference for issuers who have been subject to the periodic reporting requirements.[76]

After seeking additional comment on Rule 415, the SEC adopted it on a permanent basis in November 1983.[77] For the first time, in deference to the concerns expressed by industry participants and Commissioner Thomas, the SEC limited shelf filings for primary offerings of debt and equity securities to those made on Form S-3, as the types of offerings where "the benefits of shelf registration are most significant and where the disclosure and due diligence concerns are mitigated by other factors."[78]

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[73] *See id.* at 1161.

[74] *See* Proposed Revision of Regulation S-K and Guides for the Preparation and Filing of Registration Statements and Reports, Securities Release No. 33-6276, 46 Fed. Reg. 78, 79 (proposed Jan. 2, 1981); *see also* Adoption of Integrated Disclosure System, Securities Act Release No. 33-6383, 47 Fed. Reg. 11,380, 11,389 (Mar. 16, 1982).

[75] *See* text *supra* note 2.

[76] Over the last decade, the Commission has gone far in eliminating problems associated with duplicative disclosure obligations under the two Acts by "integrating" their disclosure requirements. This was accomplished, in part, through the adoption of Regulation S-K in 1982. In addition, the Commission has facilitated more rapid market access for seasoned companies by streamlining the registration process through the adoption, first, of Form S-16, then Form S-3, and, more recently, the creation of the "universal" shelf.

Wallman, *supra* note 12, at 2.

[77] *See* Delayed or Continuous Offering and Sale of Securities, Securities Release No. 33-6470, 48 Fed. Reg. 27,768 (Jun. 17, 1983); *see also* Shelf Registration, Securities Release No. 33-6499, 48 Fed. Reg. 52,889 (Nov. 23, 1983).

[78] One of the "other factors" that the SEC pointed to was the efficient market hypothesis. It stated that at the time that registrants on Form S-3 or Form F-3 determine to make an offering of securities, "a large amount of information already has been disseminated to and digested by the marketplace." It recognized that some commentators had said that no

The SEC cited the benefits of shelf registration, including cost savings, flexibility, simplification and increased competition among underwriters.[79] In response to the concerns of Commissioner Thomas, as well other participants in the discourse who felt that investor disclosure would suffer, the SEC argued that the integrated disclosure system enhanced the level of disclosure to investors, building on the existence of timely and accurate corporate filings and thus investors were adequately protected.[80] As for the due diligence concerns, the SEC acknowledged the potential problem, but argued that anticipatory and continued due diligence programs would assure disclosure to investors and afford underwriters an opportunity to perform due diligence.[81] However, these programs, while theoretically feasible, in reality would be very costly, in terms of time and money, and thus the concept is of limited practical value.[82]

By contrast, some commentators have argued that the introduction of the integrated disclosure system, allowing certain Exchange Act reporting companies to "incorporate by reference," and the adoption of the shelf registration process, provide investors in companies with securities in an efficient market with much of the public information available in order to make informed investment decisions.[83]

> underwriter can afford to devote the time and expense necessary to conduct a due diligence review before knowing whether it will handle an offering, and that there may not be sufficient time to do so once it is selected. The SEC pointed, on the other hand, to statements by registrants that procedures for conducting due diligence had been developed, including periodic due diligence sessions for prospective underwriters and continuous due diligence by the law firm selected to serve as underwriters' counsel.

JOHNSON, *supra* note 61, at 441; *see also* text *supra* note 2.

79 *See* Shelf Registration, 48 Fed. Reg. at 52,889.

80 *See id.* at 52892.

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> The integrated disclosure system recognizes that, for companies in the top tier, there is a steady stream of high quality corporate information continually furnished to the market and broadly digested, synthesized and disseminated. In addition, procedures for conducting due diligence investigations of such registrants, including continuous due diligence by means such as designated underwriters counsel, are being adapted to the integrated disclosure system and shelf registration. The Commission believes that the widespread market following of such companies and the due diligence procedures being developed serve to address the concerns about the adequacy of disclosure and due diligence and, thus, ensure the protection of investors.

Id. at 52892-93.

82 *See id.* at 52896 (Special Concurring Opinion of Chairman Shad).

83 *See* Choi, *supra* note 2, at 569-70 n.19. Professor Choi uses the term "efficient market" to refer to a "trading market that displays features of a semistrong efficient market . . . the semistrong version of the efficient capital markets hypothesis posits that the secondary market price of companies reflects all publicly available information on the company." *Id.* (citing Eugene F. Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383 (1970), and Donald C. Langevoort, *Information Technology and the Structure of Securities Regulation*, 98 HARV. L. REV. 747, 778-79 (1985)).

D. *The Next Public Debate*

The last stage of the cyclical model, the next public debate flowing from the continuing evaluation of the usefulness of the agency action, continues to play itself out today. The integrated disclosure system and the availability of shelf registration are universally viewed as an improvement over the prior system. The SEC has edged closer to company registration with its adoption of the universal shelf.[84] The most recent public debate centered on exploring whether the integrated disclosure system goes far enough, and, if not, how best to proceed.

Much of the prior public and agency debate still contributes to the discourse. Many of Commissioner Thomas' concerns shaped the debate on shelf registration itself, and now serve as the basis for much of the discourse on company registration, including issues such as the effect on investor protection and the ability of underwriters to accomplish meaningful due diligence.[85]

The Cohen article continues to generate discussion, even today, in that Cohen proposed the idea of company registration as part of his view on integrated disclosure.[86] Cohen's observation that the two statutes are not well integrated is almost universally accepted, yet progress towards remedying this situation in any meaningful way has been very slow.[87] Because of the cyclical nature of regulatory revision, company registration is not a revolution, but rather an evolution, flowing logically from the discourse, answering much of the debate, and yet itself generating additional debate.[88]

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[84] "The SEC, moreover, in 1992 further loosened restrictions on shelf registration, adopting the 'universal' shelf which allows Form S-3 issuers to register a specified dollar amount of securities for the shelf without allocating these securities to any particular class of securities." Choi, *supra* note 2, at 651 n.18. For a comparison of company registration and universal shelf registration, *see* SEC Advisory Committee Final Report, *supra* note 10, addendum to app. B.

[85] Coffee, among others, has argued that shelf registration has hurt the ability of underwriters and auditors to conduct their due diligence investigations. This view, however, ignores the market incentives of issuers and underwriters to find a way for underwriters to perform a certification function to the extent investors value certification. The drop in due diligence investigations, therefore, may reflect more the low value that investors place on the legal level of due diligence and less the failing of the certification mechanism.

Choi, *supra* note 2, at 651 n.67.

[86] *See* Cohen, *supra* note 38, at 1353.

[87] *See* Coffee, *supra* note 3, at 1145.

[88] Full integration, however, was not achieved and, absent legislation, arguably may never be fully achievable. Under a completely integrated disclosure system, registration under the '34 Act would suspend the obligation to register issuances of securities under the '33 Act. To date, administrative integration of the two statutes has stopped well short of this point – its

III. PROPOSED CHANGES TO THE CAPITAL FORMATION SYSTEM – COMPANY REGISTRATION

Administrative revision of securities registration continues to follow the cyclical model, bringing the securities laws ever closer to a company-based system, and further away from the complexities resulting from sustaining a transaction-based system. The current public debate focuses first on whether, and then on how, to work within the existing regulatory framework, seeking to isolate specific areas of obsolescence, and making necessary modifications.

Arguably, the Securities Act's focus on registering transactions creates unnecessary complexities for seasoned issuers already subject to the Exchange Act's continuous disclosure system. Specifically, the statutory limitations and regulatory restrictions on solicitation activities prior to and during the registration process, and concepts such as "restricted" securities and the integration of offerings, add confusion, uncertainty and costs to the capital formation process, and seem designed simply to protect the integrity of the transactional registration paradigm.[89]

A. *The Public Debate*

Since the idea of integrating the Securities Act and the Exchange Act has been around for over thirty years, participants in the public debate have had ample time to come up with criticisms and praise for the concept, as well as modifications, and, in some cases, alternatives, to company registration. Of course, different paths to integration will have different implications for the capital markets and its participants.[90]

> principal achievement being a shelf registration system under which issuers can obtain quick access to the capital markets by incorporating by reference '34 Act filings.

Coffee, *supra* note 3, at 1146.

[89] *See* Wallman, *supra* note 12, at 3.

[90] Different paths to implementation are possible and carry very different implications. In particular, the goals underlying a company registration system are multiple. For some, the aim is not simply to integrate the '33 and '34 Acts, but also to integrate public and private markets as well as to end the current system of complex and uncertain exemptions from registration under the '33 Act. At this point, the trade-offs become more complicated...although the complexity surrounding affiliate resales of issuer securities can safely be reduced, the private placement exemption has continuing value. In particular, private sales to institutional investors might constitute a preferable vehicle by which securities of some issuers should reach the public market, with institutional investors undertaking some of the risk-taking and due diligence functions formerly performed by underwriters.

Coffee, *supra* note 3, at 1147.

A significant contribution to the public debate came in May 1995, when in a prescient article, authors Backman and Kim used the concept of Securities Act metaphysics as a backdrop for a company registration proposal that is the logical extension of integrated disclosure.[91] While the Backman and Kim proposal does not go as far as the SEC Advisory Committee Final Report, it is a firm step in the right direction. According to Backman and Kim, the evolution of the securities laws, with the two statutes requiring transactional and periodic reporting, produces a metaphysical effect resulting from a hyper-technical application of Securities Act concepts in situations where the Exchange Act disclosure may already have fully informed the market.[92]

Backman and Kim propose the creation of a new registration system in which certain "seasoned" issuers could register offerings on a new form of truncated registration statement.[93] The registration statement would become effective automatically upon filing, and would, in essence, be a notification of the potential sale of securities. Upon distribution of the securities, the issuer would deliver a "prospectus" which would confirm the sale, incorporating by reference virtually all other material information. Once the offering was over, the registrant would file a form specifying the type and amount of securities sold, and would then pay a filing fee. The authors argue that their proposal improves on Form S-3's universal shelf registration, because the filing fee would not be payable unless the securities were issued, the threat of market overhang would decrease and issuers would not be required to use underwriters in a primary equity shelf offering.[94]

A major contributor to the discourse is Professor John Coffee, who has criticized the current registration system, suggesting company registration as a possible solution.[95] Professor Coffee has revisited many of the ideas in the ALI Code and in Cohen's article, updating them to take into account the many changes since the 1960s, including the dramatic increase in the number and importance of institutional investors, and the shift in trading from the

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[91] *See* Backman & Kim, *supra* note 42, at 18. In an additional bit of prescience, the authors recommend that Congress grant the SEC express exemptive authority, along the lines of § 303(a) of the ALI Code, allowing the SEC to exempt "any person, security, or transaction, or any class of persons, securities, or transactions, from any or all of the provisions of this Code." *See id.* at 21.

[92] *See id.*; *see also* McDonough, *supra* note 7, at 610-11.

[93] The proposal eliminates traditional Securities Act registration for seasoned issuers subject to the integrated disclosure system, eligible to use Form S-3 who met some minimal standard to ensure "seasoning" like listing securities on an national stock exchange or NASDAQ. The proposal retains traditional Securities Act registration for initial public offerings and certain other issuers. *See* Backman & Kim, *supra* note 42, at 20.

[94] *See id.*

[95] *See* Coffee, *supra* note 3, at 1144.

primary market towards the secondary market. Professor Coffee also notes what he calls the "development and acceptance of modern finance theory," exemplified by the efficient capital market hypothesis, and the resulting shift on the focus of disclosure from the individual to the market.[96]

Professor Coffee notes that the advantages of a company registration system to issuers include the elimination of delays, in both the preparation and filing of registration statements, and in the approval and declaration of effectiveness by the SEC.[97] Further advantages to issuers include the elimination of the "gun jumping" and "free writing" prohibitions of § 5 of the Securities Act and the elimination of the absolute rescission right granted by § 12(1), although such right may continue to exist as a matter of marketing necessity, not statutory necessity.[98] And finally, because of the material differences in the liability provisions of the Securities Act and the Exchange Act, a company registration system might provide issuers with some decrease in liability for their officers and directors due to the inapplicability of §11 liability.[99]

B. *The Agency Debate*

In recent years, the SEC staff began reexamining some of the basic concepts in the Securities Act, primarily in the area of registration

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96 In addition to his learned counsel on the costs and benefits of integration through company registration, Professor Coffee also contributed an alternative proposal to company registration, deregulating the private placement exemption. In acknowledging possible contentiousness of the public debate on company registration, Professor Coffee sets out three "ground rules" for consideration by the SEC in formulating any agency action on integration: (1) do not make company registration the exclusive registration system; (2) incentivize registrants to participate by requiring enhanced disclosure requirements on all shelf registrants, not just company registration registrants; and (3) address the liability question legislatively, cutting back § 11 liability to cover only initial public offerings and high risk issuers, and restore § 12(a)(2) liability to cover sales in the private market, as well as all offering materials used by the issuer. *See id.* at 1149.

Coffee goes on to discuss the best means of implementation of a company-based registration system, a discussion made academic by the enactment of new §§ 28 and 31 of the Securities Act and the Exchange Act, respectively. *See id.* at 1177-87.

97 *See id.* at 1155.

98 *See id.*

99 *See infra* notes 147-158 and accompanying text for a discussion of the ramifications of company registration on the liability landscape; *see also* Coffee, *supra* note 3, at 1156. Of course the benefits come at a cost, in this case, because liability is the driving force behind the quality of disclosure, investors may suffer an erosion in the quality of the disclosure provided as a result of this diminished liability. As Professor Coffee points out, this conclusion is not inevitable. The adoption of a company registration system could include an increase in the liability provisions under the Exchange Act, or an increase in the character of due diligence attention to periodic filings undertaken by an issuer's gatekeepers: accountants, directors, attorneys and other outside professionals. *See id.* at 1157.

requirements.[100] The staff's positions reflect a more literal and less flexible and pragmatic approach to applying the Securities Act.[101] This arguably has fueled the public debate on company registration, the ultimate integration of the Securities Act and Exchange Act. Components of the agency debate include an article by a high-ranking SEC official,[102] an internal task force set up by the SEC[103] and an external advisory committee, the latter two issuing reports proposing a company based registration system.

In February 1995, the SEC established the Advisory Committee on the Capital Formation and Regulatory Processes ("SEC Advisory Committee")[104]

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100 *See* Coffee, *supra* note 3, at 1153-55.

101 *See* Stanley Keller, *Basic Securities Concepts Revisited*, 9 INSIGHTS 5 (May 1995).

102 Linda Quinn, then director of the Division of Corporation Finance at the SEC, addressed the ABA's Federal Regulation of Securities Committee in the fall of 1995, presenting "a conceptual framework for identifying the problems posed by the Securities Act for these market developments and for developing and evaluating reforms to be undertaken." Her "four part approach" consisted of (i) focusing on the nature of the purchaser as one of the factors considered in defining the regulation of registered offerings; (ii) reconsidering requiring that offers be registered; (iii) reconsidering restrictions on written communications, allowing communications other than statutory prospectuses during the offering period; and (iv) reconsider prospectus delivery requirements: allowing prospectus delivery by incorporation by reference to the full prospectus, where appropriate, and pre-confirmation physical delivery of prospectuses in all other cases. *See* Quinn, *supra* note 17, at 26.

Ms. Quinn points out the voluntary aspect to Securities Act registration; issuers can choose to register offerings that would qualify as private placements and thus give their purchasers freely transferable securities, and this registration is, in essence, for the benefit of subsequent purchasers. *See id.* at 25.

According to Ms. Quinn, while requiring offers to be registered assures that information about the issuer is publicly available when the solicitations are made, exempting offers from registration would introduce significantly more flexibility and efficiency into the process. An offer would not be a § 5 event, and thus would not give rise to § 12(1) liability, but would still be subject to the anti fraud provisions, and in the case of public offerings, to § 12(2) liability. *See id.* at 26-27.

103 SEC Chairman Levitt organized the Task Force on Disclosure Simplification, an internal SEC task force, in August, 1995. The Task Force met over a seven month period with issuers, investors groups, underwriters, accountants, lawyers and others who participate daily in the capital markets. Their task was, among other things, to review forms and rules relating to capital-raising transactions. Specifically, the SEC Advisory Committee's objective was:

> [T]o assist the Commission in evaluating the efficiency and effectiveness of the regulatory process and the disclosure requirements relating to public offerings of securities, secondary market trading and corporate reporting, and in identifying and developing means to minimize costs imposed by current regulatory programs, from the perspective of investors, issuers, the various market participants, and other interested persons and regulatory authorities.

Charter of the Securities and Exchange Commission Advisory Committee on the Capital Formation and Regulatory Processes (February 24, 1995, renewed February 21, 1996) *at* http://www.sec.gov/news/studies/capform/capffull.txt (last visited Feb. 28, 2001).

104 The SEC Advisory Committee consisted of: Commissioner Steven M.H. Wallman, John C. Coffee, Jr., Barber B. Conable, Jr., Robert K. Elliot, Edward F. Greene, George N. Hatsopolous, A. Bart Holaday, Paul Kolton, Roland M. Machold, Burton G. Malkiel, Claudine Malone, Charles Miller, Karen M. O'Brien, and Lawrence W. Sonsini. *See* Securities Acts Concepts and Their Effects on Capital Formation, Securities Act Release No. 33-7314, 61 Fed. Reg. 40,044 at 40,044 n.7 (July 31, 1996).

to advise it regarding "informational needs of investors and regulatory costs imposed on the U.S. securities markets."[105] In the course of its work, the SEC Advisory Committee identified various regulatory uncertainties, complexities and anomalies in the existing system, stemming primarily from efforts to adapt to current market developments, that it believed would ultimately impact the system's ability to protect investors.[106]

The SEC Advisory Committee determined that the current procedures under the Securities Act were well suited to initial public offerings of securities, but not as well suited to issuances of securities by public companies currently filing reports under the Exchange Act.[107] Accordingly, in its final report to the SEC, the SEC Advisory Committee proposed adopting company registration,[108] unanimously recommending that the SEC "act promptly both to strengthen existing investor safeguards and to reduce the costs of corporate capital formation in the United States by establishing a company registration system."[109]

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[105] *See* Charter of the Securities and Exchange Commission Advisory Committee on the Capital Formation and Regulatory Processes (February 24, 1995, renewed February 21, 1996) *at* http://www.sec.gov/news/studies/capform/capffull.txt (last visited Feb. 28, 2001).

[106] *See* Transmittal Letter for the Final Report of the Advisory Committee on the Capital Formation and Regulatory Processes (July 24, 1996) *at* http://www.sec.gov/news/studies/capform/capffull.txt (last visited Feb. 28, 2001).

[107] *See* SEC Advisory Committee Final Report, *supra* note 10, at i-ii.

[108] Company registration would further the traditional goals of the disclosure requirements under the federal securities laws – to provide investors with the information necessary to make an informed decision and to deter fraud and overreaching. While company registration would maintain and in some cases expand the level of information about companies and their offerings that currently is made available to the markets through Commission filings, such information would be required to be made public earlier than under the current system, thereby benefiting investors in both the primary issuance market and the secondary trading markets. At the same time, company registration would afford companies offering their securities to the public the flexibility to tailor the disclosure documents delivered to investors to the nature of the transaction and the demands of the offering participants. Company registration also would maintain and reinforce the roles of outside gatekeepers and monitors and their due diligence functions in fostering the reliability of that information to meet the realities of today's markets.

SEC Advisory Committee Final Report, *supra* note 10, app. B.

[109] *See* Transmittal Letter for Final Report of the Advisory Committee on the Capital Formation and Regulatory Processes, *supra* note 106.

> The Committee believes that the cumulative effect of the evolutionary changes in the markets since the 1930s now require a reassessment of the conceptual underpinnings of the regulatory process, as opposed to continued incremental changes. Company registration is consistent with the evolutionary approach of incremental liberalization, but it is also, unmistakably, a new departure. Unlike incrementalism, it says with finality that registration should not take precedence over periodic disclosure for companies that are already traded. It recognizes and addresses what was not yet apparent in the early 1930s: the economic importance of traded

Under company registration as proposed by the SEC Advisory Committee ("SEC Advisory Committee Proposal"),[110] to become "company-registered," eligible companies would file a Form C-1 registration statement "disclosing plans to make offerings from time to time on a company-registered basis and registering all sales of all securities."[111] The Form C-1 would be kept current by incorporating all existing and future Exchange Act filings therein.[112] The Form C-1 would contain a generic description of the types of securities the issuer was contemplating issuing, and a general discussion of the issuer's financing plans.[113] Thus the Form C-1 would not be a single document, but rather a composite of the initial C-1, plus all Exchange Act filings incorporated in by reference as well as any post-effective amendments thereto.[114] A "pay as you go" system for fees would result from the nominal fee paid upon filing, with an undertaking to pay a fee upon each sale of security under the Form C-1.[115]

Under company registration, all purchasers of securities from the issuer or its affiliates would receive freely transferable securities, regardless of the nature of the transaction.[116] Likewise, they would benefit from all of the statutory remedies connected with the dissemination of information in a

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> companies raising additional capital by issuing securities. Thus company registration is far more than a cost-reduction and efficiency reform. It is a new beginning for the registration process, and it is overdue. The shift to a company registration system thus would change the way we think about the regulation of the capital formation process and foster a fresh approach to addressing the various problems. This more comprehensive conceptual approach would address both the interests of seasoned issuers in today's fast-moving markets and offering processes for investors, underwriters, and other participants.

SEC Advisory Committee Final Report, *supra* note 10, at 51-52.

110 Under the SEC Advisory Committee Final Report:

> Registration is company, not transaction-based (except IPOs and other specific transactions). Once meeting eligibility standards, companies register with the SEC and file periodic reports. Routine financings, as well as resales by affiliates and resales of what are currently known as restricted securities, could be consummated without the current SEC review and registration process. Information provided to investors in the marketing of these routine financings would be based on what the market demands and on company and transactional information required to be filed as part of the issuer's periodic reports. The principal distinctions currently existing between public and nonpublic offerings by registered companies (with the resulting formalities and restrictive concepts such as gun-jumping and integration) would be eliminated, because offers and sales by companies already registered with the SEC generally would not be subject to additional transactional registration requirements.

SEC Advisory Committee Term Sheet, *supra* note 22, at 1.

111 *See* SEC Advisory Term Sheet, *supra* note 22, at 2.

112 *See* SEC Advisory Committee Final Report, *supra* note 10, at 7.

113 *See id.*

114 *See id.*

115 *See id.* at 8.

116 *See id.* at 9.

registered offering.[117] Accordingly, investor protection would be preserved and in fact, extended to a broader class of transactions, while eliminating unnecessary concepts like gun-jumping, and restricted securities.[118]

The goals of the SEC Advisory Committee Proposal are to:

- improve the protection of investors in the primary offering market;
- reduce the cost of capital formation, eliminate unnecessary regulatory costs and uncertainties that currently impede a company's access to the capital markets, and streamline and simplify the process of raising capital;
- enhance the disclosure provided to investors in the secondary trading markets on an ongoing basis, not just when the issuer determines to conduct a public offering; and
- eliminate complexities arising from the need to distinguish between public and private, domestic and offshore, and issuer and non-issuer transactions.[119]

Within these goals are echoes of the themes of the last thirty years of public debate, from Cohen, to the ALI Code, to Coffee. Throughout the debate, some have questioned whether the current registration requirements establish unnecessary obstacles to capital formation, without any compensating benefits to investors, especially with respect to complex concepts like "restricted" securities, integration of offerings and limitations on general solicitation, all of which arguably exist to protect the core paradigm of transaction registration.[120] The SEC Advisory Committee Proposal answers many of these questions, facilitating access to capital markets, easing the complex and technical regulatory concepts, and increasing the amount and quality of disclosure provided to investors.[121] Of

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117 *See id.*

118 *See id.*

119 SEC Advisory Committee Final Report, *supra* note 10, at 1-2.

120 *See* Wallman, *supra* note 12, at 3.

121 At least one commentator argues that the company registration system Milton Cohen envisioned is, in substance, "already largely in place within the present securities regulatory framework." *See* Choi, *supra* note 2, at 569. Professor Choi instead argues that reform within the current regulatory framework, specifically the institution of a status-based anti-fraud liability standard, would more easily achieve the goals of the SEC Advisory Committee's proposals. *See id.* at 571. "Moving toward a status-based antifraud regime, moreover, would leave most of the current system's existing framework in place, avoiding the confusion inherent in shifting to a completely new regulatory paradigm." *Id.* at 572.

According to Professor Choi:

The Advisory Committee's recommendations, although appealing on a theoretical level, are largely peripheral to creating a company registration system. The Article supports this

course not everyone agrees with the SEC Advisory Committee's recommendations.[122]

Company registration would streamline the process of accessing the capital markets. The offering process would be simplified since offerings could be tied to the issuer's need for capital, not to the regulatory environment. Additionally, market considerations, not regulatory concerns, would govern an issuer's timetable because eliminating the preparation and filing of a Securities Act registration statement, as well as eliminating the wait for SEC approval and declaration of effectiveness, would diminish delay, cost and uncertainty to the process.[123] Issuers would have more flexibility to

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> proposition by demonstrating that reforms instituted during the 1980s already introduced most of the substantive benefits of a company registration system within the Securities Act. Furthermore, those Advisory Committee recommendations that more directly introduce a pure company registration system are both unsuitable for non-S-3 companies and provide only incremental substantive changes to the current regime . . . status-based antifraud and company registration reform . . . achieve[s] at a lower cost many of the incremental benefits that company registration provides for the current system.

Id. at 573.

The three SEC Advisory Committee members, writing a separate statement to the Final Report of the Advisory Committee on the Capital Formation and Regulatory Processes, also focus on liability concerns, but according to Professor Choi, their focus is almost entirely centered on clarifying the due diligence requirements gatekeepers like underwriters, outside directors and accountants. *See* Choi, *supra*, note 2, at 651 n.21; *see also* SEC Advisory Committee Final Report, *supra* note 10, at 53 (Separate Statement of John C. Coffee, Jr., Edward F. Greene, and Lawrence W. Sonsini).

According to Professor Choi,

> [T]the level of antifraud liability for primary issuer transactions should turn on the status of the issuer and not on the type of transaction...where the issuer is a Form S-1 company, possessing little market experience and few market-based deterrents against fraud, it should be subject to the most stringent level of antifraud liability regardless of the type of transaction it undertakes. Conversely, Form S-2 and S-3 issuers, who are presumptively better followed and more highly capitalized, should face lower levels of antifraud liability.

Choi, *supra* note 2, at 572-73.

[122] The SEC Advisory Committee Final Report "presents a curious mixture of proposals directly related to creating a company registration system and other proposals not necessarily dependent on company registration." See Choi, *supra* note 2 at 616.

[123] *See* SEC Advisory Committee Term Sheet, *supra* note 22, at 19.

> At its heart, the Advisory Committee's proposed company registration system establishes a form of continuous shelf registration system. Companies entering the company registration system are required to file a new Form C-1 with the SEC containing "a generic description of the type of securities the issuer anticipated issuing, as well as a general discussion of its financing plans." After the initial filing of Form C-1, the information in the Form C-1 would be kept current by incorporating all existing Exchange Act filings, including Form 10-K, 10-Q, and 8-K filings. The continuous registration statement for Section 5 and Section 11 purposes then consists of the original Form C-1 and all incorporated documents.

Choi, *supra* note 2, at 616.

go to the market more often, for lesser amounts, because of the lower transaction cost and the decrease in time delays.[124]

Company registration would further the stated goals of the Securities Act and the Exchange Act[125] by providing investors with information necessary to make informed decisions and to deter both fraud and overreaching on the part of issuers.[126]

Issuers would have greater flexibility in determining the nature of their marketing efforts since the timing and content of prospectuses would be driven by marketing considerations (subject to the anti-fraud provisions), instead of by SEC rule.[127] The SEC Advisory Committee Proposal divides transactions into three levels, routine,[128] non-routine[129] and extraordinary,[130]

> The two main benefits claimed by the Advisory Committee over today's shelf registration under Rule 415 are that: "The current limitations of the shelf registration system on the amount of securities that could be registered would be eliminated, as would the need to file a new registration statement to register additional securities." Rule 415 currently allows S-3 companies to register only up to 10 percent of a company's outstanding voting equity for "at the market" offerings; furthermore, the company must reasonably expect to issue its shelf-registered equity within two years of its registration.

Id. at 651 n.179, (quoting SEC Advisory Committee Final Report, *supra* note 10, at 9; Rule 415, 17 C.F.R. § 230.415)(1999)).

124 *See* SEC Advisory Committee Term Sheet, *supra* note 22, at 19-20.

125 *See supra* notes 8-9 and accompanying text.

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> While company registration would maintain and in some cases expand the level of information about companies and their offerings that currently is made available to the markets through Commission filings, such information would be required to be made public earlier than under the current system, thereby benefiting investors in both the primary issuance market and the secondary trading markets. At the same time, company registration would afford companies offering their securities to the public the flexibility to tailor the disclosure documents delivered to investors to the nature of the transaction and the demands of the offering participants. Company registration also would maintain and reinforce the roles of outside gatekeepers and monitors and their due diligence functions in fostering the reliability of that information to meet the realities of today's markets.

SEC Advisory Committee Final Report, *supra* note 10, app. B.

127 *See id.* "Delivery of the transactional information could be accomplished either by incorporation by reference or by actual delivery, depending on the size of the offering and other factors. The prospectus would not be subject to prior staff review except in the case of 'extraordinary' securities transactions." *Id.*; *see also* Coffee, *supra* note 3, at 1155.

128 Under the Term Sheet for the Pilot Company Registration Program "routine" transactions are deemed to fall within Tier One:

> In "routine" transactions, an issuer could incorporate information in the Form C-1 registration statement and filed reports, including the transactional information filed on a Form 8-K, into a document serving as the prospectus, such as the confirmation or selling materials, that is then distributed to investors, thereby satisfying in any of these cases the prospectus delivery requirements.
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> . . . .

and determines the need for prospectuses as a function of the informational needs of the investors, not the need to prepare and deliver after-the-fact compliance documents determined by the SEC.[131]

Under company registration, transactional information would still need to be physically delivered as part of the prospectus when delivery of such information arguably might serve to facilitate an investor's evaluation of the issuer or the security offered.[132] But if such delivery is not necessary in order to facilitate the investor's evaluation, and where the information has already been disclosed to the markets through a public filing made with the SEC, company registration provides the flexibility for issuers to file the information with the SEC without physical delivery to investors.[133]

Company registration would also ease some of the complex and technical regulatory concepts that can delay or block access to the capital markets.[134] The need to differentiate between freely transferable securities issued pursuant to a registration statement and "restricted" securities issued in some exempt transactions would, in most cases, disappear, along with the concepts of "integration" and "general solicitation," providing liquidity benefits to

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> Any material company developments to be incorporated must be filed on the Form 8-K a reasonable time prior to the dissemination of the prospectus incorporating the information (e.g., one to three business days) to provide the market an opportunity to absorb the information. Otherwise, as today, the information must be delivered physically as part of the formal prospectus, which is filed simultaneously with the Commission.

SEC Advisory Committee Term Sheet, *supra* note 22, at 5-6.

[129] Under the Term Sheet for the Pilot Company Registration Program "non routine" transactions are deemed to fall within Tier Two and consist of "any single transaction increasing, or potentially increasing, the issuer's outstanding voting securities by more than 20%." *Id.*

> In "non routine" transactions, the issuer would be required to prepare and deliver a formal prospectus containing transactional and, where appropriate to update disclosures, company information. The prospectus would be filed (in addition to or as part of the mandated Form 8-K in non-de minimus equity offerings) with, but would not be subject to registration or prior review by, the SEC. Information previously provided in selling materials need not be redelivered.

Id. at 6.

[130] Under the Term Sheet for the Pilot Company Registration Program "extraordinary" transactions are deemed to fall within Tier Three and include "any financing, merger, material acquisition or other restructuring transaction involving a company's issuance of securities that results in an increase, or potential increase, of at least 40% of the outstanding voting share." *Id.* at 6-7. "In 'extraordinary' transactions, a post-effective amendment to the Form C-1 would be required and would be subject to SEC staff review of the transactional information. The same prospectus delivery requirements as in Tier Two transactions would apply." *Id.*

[131] *See* Coffee, *supra* note 5, at 1155.

[132] *See* SEC Advisory Committee Final Report, *supra* note 10, app. B.

[133] *See id.*

[134] *See* SEC Advisory Committee Term Sheet, *supra* note 22, 19-20.

investors for what would otherwise be privately placed securities.[135] These constructs arguably have developed over the years in an effort to maintain the separation of the public and private markets, which are less necessary under company registration.[136] The approach the SEC selects to implement the program will influence its success in eliminating these complexities.[137]

Under the SEC Advisory Committee Proposal, the transition to company registration would be accomplished by a pilot program, available only to larger, more seasoned issuers with specified minimum public floats and reporting histories, reducing the number of possible participants to thirty percent of public companies, who will serve as a test of the logistics of the program before it is opened up to all issuers.[138] The SEC Advisory Committee recommended that based on the experience with the pilot, the SEC could then decide what additional conditions or modifications need be made to the program.[139]

The SEC Advisory Committee Proposal contains a provision called company "lite," under which issuers could elect a modified company registration that would continue to permit private placements of any of its securities, including equity securities, as well as reliance on other transactional exemptions, as long as such issuers undertook to adopt the enhanced disclosure practices.[140] This arguably political accommodation will

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135 *See* Wallman, *supra* note 12, at 3.

136 *See* SEC Advisory Committee Term Sheet, *supra* note 22, at 20.

137 *See infra* notes 138-142 and accompanying text for a description of the SEC Advisory Committee's proposed method for implementing company registration.

138 According to the SEC Advisory Committee:

> The Committee determined that a pilot company registration program would be the most appropriate way to begin the transition. The pilot would be available initially only to issuers that meet certain criteria, such as having a specified minimum public float and reporting history. Because these issuers generally are more sophisticated with respect to financial reporting and other disclosure requirements and are more widely followed by the markets, the Committee concluded that permitting these types of issuers to opt into the pilot program would provide the best test of the advantages of the company registration system as compared to the current system.

SEC Advisory Committee Final Report, *supra* note 10, at iv, 41; *see also* SEC Advisory Committee Term Sheet, *supra* note 22, at 9.

139 *See* SEC Advisory Committee Final Report, *supra* note 10, at iv.

140 With modified company registration, or company "lite," as long as the issuer complies with the enhanced disclosure practices, the issuer would have the benefit of the "pay as you go" registration process for its public offerings. Exempt sales would not be integrated with registered sales made under the company registration system. But the privately placed securities would be restricted.

The modified company registration allows issuers to evaluate the benefits of registration of all equity sales against the benefits of a continued private placement exemption, including the absence of § 11 liability for sales under the private placement exemption. *See* SEC Advisory Committee Term Sheet, *supra* note 22, at 12-13.

serve to encourage issuers to participate in the pilot program. The SEC Advisory Committee believed that, despite the added complexities stemming from company "lite," the provision was necessary as an incentive to get issuers to participate at all, allowing them time to become comfortable with the concept of company registration.[141] However, the drawback to the flexibility of offering a company "lite" option is that if the program is voluntary, and some eligible issuers elect not to participate, the potential benefits of the concept of company registration from eliminating such complexities as restricted securities might not be fully realized.[142]

Company registration should improve the quality of disclosure provided by issuers to both the primary and secondary trading markets.[143] Historically, the quality of disclosure under the Securities Act has exceeded that of the Exchange Act.[144] The required disclosure enhancements, including the

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141 *See* SEC Advisory Committee Final Report, *supra* note 10, at 34-35.

142 Hopefully, the market will drive issuers to the most efficient option.

> The incentives to opt into a company registration system are uncertain and limited. Some companies may prefer to rely on the existing shelf registration system. In our judgment, it is unwise to have two parallel systems, one carrying the obligation to file a mandatory Form 8-K at the time of a substantial equity issuance plus requirements for certification by top management and the preparation of a senior management report; and the other, not. Any disparity between company registration and shelf registration that requires mandatory filings, certifications, and reports under the former (but not the latter) will create an unfortunate and powerful incentive for issuers to opt to remain within the existing shelf registration system. Thus, we would urge the Commission to adopt similar requirements with respect to the existing shelf registration system.

SEC Advisory Committee Final Report, *supra* note 10, at 54 (Separate Statement of John C. Coffee, Jr., Edward F. Greene, and Lawrence W. Sonsini).

The Committee's approach is similar in effect but different in concept from the way the SEC adopted shelf registration, adopting the rule on a temporary basis to give issuers and market participants a chance to further comment on the program, while itself gathering data to help it assess the success of the program.

143 At least for companies in an efficient market, one of the greatest advantages of a company registration system is its elimination of the need to register repeatedly securities of the same class. Because entire companies are registered, investors may freely purchase any security of the registered company; rather than becoming a focal point for regulation and disclosure, primary transactions simply are treated as any other major information event... [But] as the cost of conducting repeated registrations of securities diminishes – through shelf offerings, for example – this advantage of formal company registration diminishes. Likewise, a true company registration system would similarly restrict the trading of securities of lightly followed companies with little public information regardless of the path the securities took to market. The Advisory Committee, however, does not examine this possibility, instead focusing exclusively on the implications of company registration for companies trading in an efficient market only.

Choi, *supra* note 2, at 608.

144 The expense of continuous due diligence of the caliber expected in primary distribution, coupled with the issuers' legitimate need to control the timing of public disclosure of material

formation of disclosure committees, enhanced involvement by senior management, and improvements in the content and timeliness of Exchange Act reporting, should result in more careful due diligence practices, raising the level of all corporate disclosure.[145]

As is the case with any proposed solutions to complex problems, the "solution" of company registration remedies some problems, and arguably generates some of its own, such as the appropriate standard of liability and the ability of underwriters to undertake meaningful due diligence.[146] Company registration would affect the current liability landscape,[147] which itself has undergone changes in recent years.[148] The Supreme Court decision

> developments, make it difficult for Exchange Act documents always to achieve true parity in terms of reliability and currency with documents filed in connection with registered offerings. However, the Committee believes that additional improvements in Exchange Act disclosure—especially with respect to the attention paid by senior management, outside directors and other gatekeepers or monitors— would achieve more fully the intent of the Commission when it integrated the disclosure requirements of the two statutes in 1982.

SEC Advisory Committee Final Report, *supra* note 10, at 67-68.

[145] According to the SEC Advisory Committee, "complementing measures to ease issuer access to the market would be measures to improve the level and reliability of secondary market disclosures." *See* SEC Advisory Committee Term Sheet, *supra* note 22, at 13.

The disclosure enhancements include (a) certification to the SEC by two of the following four officers: CEO, COO, CFO or CAO, certifying that they have reviewed the Exchange Act filings and are not aware of any misleading disclosures or omissions; (b) reports prepared by management and submitted to the audit committee, describing the procedures used to ensure the integrity of the Exchange Act filings, and describing procedures instituted to avoid insider trading; (c) expanded reporting obligations under Form 8-K for disclosures of items previously required to be filed quarterly, and under company registration, must be filed on a current basis; (d) risk factor analysis disclosure requirements required in Securities Act filings would be added to Form 10-K. *See* SEC Advisory Committee Term Sheet, *supra* note 22, at 14.

[146] Requiring Securities Act-type due diligence on Exchange Act filings will be vastly more expensive for the issuers.

[147]
> This approach does not represent a change in the liability system for public offerings (with the exception of sales by persons who would no longer be subject to resale restrictions and thus who would not have liability under Section 11 for their resales), but represents an expansion of liability to the extent transactions that would otherwise be exempt private placement or flowbacks from overseas placements are covered by the Form C-1. In addition, because in many offerings the transactional information will be filed on Form 8-K and made part of the registration statement, rather than merely part of a prospectus supplement as is the practice in shelf offerings today, Section 11 will apply to that disclosure when it has not been applicable under the current scheme.

SEC Advisory Committee Term Sheet, *supra* note 22, at 16.

[148] "The Supreme Court has partially reaffirmed this conclusion by refusing to extend the strict and vicarious liability provisions of the 1933 Act to private placements, a fast-growing method for issuers to bypass traditional 1933 Act registration." McDonough, *supra* note 7, at 563 n.9 (citing Gustafson v. Alloyd Co., Inc., 513 U.S. 61, 64 (1995)).

in *Gustafson v. Alloyd Co., Inc.*,[149] holding that the negligence standard of § 12(a)(2) of the Securities Act applies only to public offerings, arguably weakens the Securities Act disclosure scheme. At the same time it provides the basis to strengthen the Exchange Act disclosure schemes, through the mechanism of company registration.[150]

Company registration "will preserve the current statutory liability provisions, in that § 11 will continue to be applied in a manner similar to its current application."[151] Issuers, officers, directors, experts and underwriters would be vulnerable to § 11 liability for false or misleading statements in the Form C-1, including all the information incorporated by reference from the Exchange Act filings.[152] Of course, defendants other than issuers would still be able to avail themselves of the due diligence defense.[153] In addition, company registration will expand the coverage of § 11 to transactions that are currently undertaken without registration, such as private placements and offshore offerings.[154]

Company registration will decrease liability exposure for some issuers, through the elimination of the § 12(a)(1) absolute right of rescission for an investor who did not receive a prospectus prior to the mailing of the confirmation or delivery of shares. But issuers that might otherwise have offered securities through a private placement, when making a public offering under company registration, would become subject to § 11 and § 12(a)(2) liability.[155]

Under the shelf registration system, issuers who provide transactional disclosure through a prospectus supplement rather than a filing included in a registration statement, deny their investors the protection of § 11 with respect to such disclosures. Some commentators argue that seasoned issuers

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149 513 U.S. 61 (1995).

150 *See* Margaret A. Bancroft, *Responding to Gustafson: Company Registration and a New Negligence Standard*, 9 INSIGHTS 14 (Jul. 1995).

151 *See* SEC Advisory Committee Final Report, *supra* note 10, app. B.

152
> The issuer would be subject to strict Section 11 liability to purchasers of securities sold under the company registration statement for materially false or misleading information in the Form C-1 (including all incorporated information such as transactional information filed as part of the Form 8-K). Officers, directors, experts and underwriters likewise would be liable for materially false and misleading statements in the Form C-1 (including transactional and updating information filed on the Form 8-K and incorporated into the Form C-1) and any post-effective amendments thereto (with due diligence defenses afforded under current law).

SEC Advisory Committee Term Sheet, *supra* note 22, at 16; *see also* SEC Advisory Committee Final Report, *supra* note 10, app. B.

153 *See* SEC Advisory Committee Final Report, *supra* note 10, app. B.

154 *See id.* at 86.

155 *See* Coffee, *supra* note 3, at 1156, for a discussion of the reduction in liability exposure for issuers and their officers and directors under company registration.

that could raise capital in reliance on their Exchange Act filings, without registration under the Securities Act, should be held to some new Exchange Act negligence standard.[156] This is unnecessary under company registration, because the pilot program requires that transactional information disclosed in a Form 8-K must be incorporated into the registration statement and therefore would come within the coverage of § 11.

The SEC Advisory Committee considered several alternative liability schemes[157] but ultimately advised retaining the current liability scheme, at

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[156] Any new negligence standard needs to strike a balance between investor protection and company protection from strike suits and frivolous litigation. One means of striking a balance would be to provide a safe harbor to those registrants who engage independent accountants and law firms to actively review, comment on, and revise key Exchange Act documents, including 10K's and 10Q's, in advance of their filing. The point of the active, participatory auditor/lawyer review would be to replicate, to the extent practical, the valuable, critical review process associated with long-form Securities Act filings.

> Because company registration reflects the ultimate ascendancy of Exchange Act disclosure over that of the Securities Act, it should incorporate some of the rigor of the Securities Act in policing disclosure. Therefore, company registration should be offered to issuers only on the condition that they agree to be governed by a new negligence standard for Exchange Act filed documents that replaces the dead letter of Section 18 of that Act. This would strengthen the federal disclosure system as it relates to both the trading and the capital raising markets. The new negligence standard could be modeled on the Section 12(2) formulation of negligence, with appropriate modifications designed to recognize that the new standard would provide a civil remedy for purchasers of a company's securities in the open market, as well as in capital raisings. For example, as is the case with the American Law Institute's Federal Securities Code, a cap could be placed on the maximum liability of any defendant.

Bancroft, *supra* note 150, at 15-16.

The approach taken by the SEC, should it adopt company registration, also bears on the liability issue. If company registration is optional, issuers could essentially opt out of a new liability standard by registering under the Securities Act:

> [A]nd investors, given the choice of accepting privately placed shares policed solely by Rule 10b-5's fraud remedy or company registered shares policed by a negligence standard, might very well help issuers decide that company registration was a viable option by demanding premiums for privately placed securities. In addition, greater public confidence in the integrity of Exchange Act filings could favorably affect the trading price of securities of companies that choose company registration. Ironically, *Gustafson* which weakens the Securities Act disclosure system may serve as the force that finally puts the Exchange Act at the center of federal securities regulation.

Id. at 15-16.

[157] The SEC Advisory Committee considered (i) issuers would incur § 11 liability on for initial public offerings and extraordinary distributions, and § 12(a)(2) liability for routine transactions; (ii) extending §§ 11 and 12(a)(2) remedies to all purchasers in primary offerings and in secondary market transactions contemporaneous with the offering, limiting the issuers total liability to the lesser of the offering proceeds or the damage caused, with the awarded damages prorated among investors in the primary and secondary markets; (iii) eliminating § 11 liability and extending § 12(a)(2) liability to all statements made by the issuer, regardless of whether the issuer was selling securities or if its securities

least for the pilot phase of the program, "to maintain important investor protections while achieving the objectives of company registration," with the proviso that relevant parties be given additional guidance on the factors relevant to establishing a due diligence defense under § 11 and § 12(a)(2).[158]

A related concern arising out of company registration stems from the ability of underwriters to undertake due diligence. This concern was raised in connection with shelf registrations by Commissioner Thomas in her dissent to the adoption of Rule 415, and is still a part of the debate.[159] Company registration will also increase the effectiveness and quality of due diligence.[160]

With the accelerated timing of offerings under company registration, the underwriters may be selected very near the time of sale and therefore have little or no time to complete any meaningful due diligence. The SEC Advisory Committee declined to recommend limiting liability for gatekeepers and monitors, and instead recommended providing more guidance, within Rule 176, to elaborate on what constitutes "reasonable investigation" and/or "reasonable care" for purposes of the due diligence defense in §§ 11 and 12(a)(2) under company registration.[161] The underwriting community will likely not be greatly comforted by this approach, seeking instead to have its liability reduced.

C. *The Agency Proposal*

After receiving the report of the SEC Advisory Committee, the SEC published a concept release seeking comment on possible reforms to further its investor protection mandate and to reform the current regulation of the

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were trading in the secondary market; (iv) limiting liability for a registered company's routine financings to Rule 10b-5 liability only. *See* SEC Advisory Committee Final Report, *supra* note 10, at 88.

158 *See* SEC Advisory Committee Final Report, *supra* note 10, at 87.

159 *See* Examination of the Registration of Securities to be Offered and Sold on a Delayed or Continuous Basis in the Future, Securities Release No. 33-6391, 47 Fed. Reg. 11,701 (Mar. 18, 1982)(Commissioner Thomas dissent). *But see* Barbara Ann Banoff, *Regulatory Subsidies, Efficient Markets, and Shelf Registration: An Analysis of Rule 415*, 70 VA. L. REV. 135 (Mar. 1984)(arguing that the improvements in information getting to the market through the underwriters' due diligence does not really benefit investors, obviating the need for due diligence); Merritt B. Fox, *Shelf Registration, Integrated Disclosure, and Underwriter Due Diligence: An Economic Analysis*, 70 VA. L. REV. 1005 (Jun. 1984)(for a defense of the information improvement resulting from due diligence); American Bar Association Committee on Federal Regulation of Securities, Report of the Task Force on Sellers' Due Diligence and Similar Defenses Under Federal Securities Law, 48 BUS. LAW. 1185 (May 1993).

160 *See* SEC Advisory Committee Final Report, *supra* note 10, app. B.

161 *See* SEC Advisory Committee Final Report, *supra* note 10, at 96.

capital formation process.[162] The SEC undertook to consider public comment on the recommendations in the SEC Advisory Committee Proposal, and other ideas in the release before taking any agency action.[163]

D. *The Renewed Public Debate*

The SEC received over sixty comment letters, covering a range of issues from timing considerations, feasibility of disclosure enhancements and concerns about liability and due diligence issues.[164] The SEC has yet to act on the proposal or comments thereto.

The concept of company registration put forth in Cohen's article has been refined and developed through public and agency debate over the last thirty years, with renewed interest beginning in the mid-1990s. The prior debates on the complete integration of the Securities Act and the Exchange Act have contributed to, if not actually precipitated, the SEC's adoption of the integrated disclosure system, and the shelf registration process. The renewed public debate on the company registration proposal will no doubt have an impact on any agency action and its aftermath. But the debate is far from over, and, as it continues, it will likely focus substantively on the appropriate liability standards, and practical resolutions to the due diligence timing issues, and, procedurally, on the wisdom and practicality of a voluntary program.[165] This debate will lay the groundwork for additional

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[162] *See* Securities Act Concepts and Their Effects on Capital Formation, Securities Release No. 33-7314, 61 Fed. Reg. 40,044, 40,044-45 (Jul. 25, 1996).

[163] *See id.*

[164] The comment letters addressed both the SEC Advisory Committee Final Report and other components of the public and agency debate. Nine of the comment letters dealt simply with mechanics, such as requests to extend the comment period. Eight of the fourteen SEC Advisory Committee members submitted comments, primarily in the form of transcripts of their testimony before the SEC. Other commenters included lawyers and bar associations, accounting firms, investment banks and securities trade institutions and corporations. *See* Dominic Bencivenga, *'33 Securities Act at 64; Update Seen Needed, But How Far Should It Go?* N.Y.L.J., Feb. 20, 1997, at 5.

[165] "Progress toward company registration is possible, and the time is ripe. Much of the debate, however, necessarily will focus more on the means than on the ends." Coffee, *supra* note 12, at B4.

> If a company is registered and reporting under the Exchange Act, there should not be the impediment to a registered or unregistered offering that § 5 creates. The Wallman Committee has suggested that company registration should be the statutory goal, but pending proposals of the Wallman Committee will not solve the problems encountered by small and mid-size companies.
>
> Although new registration forms are being developed to accomplish company registration, as opposed to securities registration, these new forms will be for seasoned issuers only. Further, a company will have to opt into the new scheme and voluntarily agree to several enhancements to current disclosure practices . . . . The objective of these enhancements will be to enhance the integrity, but not the scope of disclosure. Yet, it is not clear what the cost

agency action and public debate thereon.[166]

IV. CONCLUSION

Company registration is the logical culmination of years of public debates, agency debates, agency proposals and agency actions that began with the unfortunate enactment of two separate statutes, resulting in duplicative and onerous disclosure obligations. These debates, proposals and actions have taken the securities laws through the adoption of the integrated disclosure system and the adoption of the streamlined shelf registration process. Although a proposal such as company registration could be seen as an abandonment of the current system, a better explanation is that company registration is a sensible next step, flowing logically from the prior debate, and from the continued lack of statutory integration and the conflict resulting therefrom.

The SEC has the statutory authority to continue these trends, by shifting our current system of registering securities away from a transaction-based system and towards a company-based system. The SEC Advisory Committee generated a viable blueprint towards this goal with their Final Report in 1996.

> or liability implications of these enhancements would be .... Nevertheless, the current system is a regulatory tax on capital formation in increasingly competitive international capital markets. While investor protection against fraud is clearly necessary to preserve investor confidence and to create a healthy climate for capital formation, modern communications and technology should make it possible for both private placements and underwritings to proceed in a less cumbersome way than under current § 5 law and regulation.

Karmel, *supra* note 7, at 3.

[166] To the extent that the SEC pursues a voluntary company registration model administratively, it must avoid the danger of allowing the costs associated with this option to exceed its benefits. A model that is exclusive – that is, that denies those electing it the ability to use private placements or Regulation S for equity sales – has real costs compared with less certain benefits. Not surprisingly, then, there are already signs that the principal constituencies affected by SEC actions are uncertain to skeptical about the benefits of company registration. Underwriters fear it will lead to further erosion in due diligence and their gatekeeper role, while issuers do not like the obligation to register sales by affiliates and the "flow back" from foreign offerings, plus the risk of Section 11 liability. To be sure, these expressed reservations may partially mask other concerns; for example, underwriters may fear loss of their special relationships to the traditional issuer clients and dislike increased competition, while issuers may simply want additional "sweeteners." Nonetheless, they suggest the need to rethink the process of administrative implementation.

Coffee, *supra* note 3, at 1185-86.

Professor Coffee made three final recommendations: (1) the SEC should avoid exclusivity, making company registration one of several options; (2) the costs of company registration should be taxed to shelf registrations and not to the use of some new universal shelf registration statement; and (3) issues of liability should be addressed legislatively. *See id.* at 1186-87.

Now is the time to start additional public debate and discourse on this critically important issue, to bring to light any logistical problems in the SEC Advisory Committee Proposal and pilot plan, and to generate any necessary solutions. The SEC should have the strength and the foresight to recognize the need for reform in the way we register securities, and to use its rulemaking authority to move the system towards company registration.