



By Electronic Mail (rule-comments@sec.gov)

March 18, 2011

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Security Ratings; Release No. 33-9186; 34-63874; File No. S7-18-08

Dear Ms. Murphy:

The Capital Markets Committee of the Securities Industry and Financial Markets Association (“SIFMA”) welcomes this opportunity to respond, on behalf of SIFMA, to the request for comments by the Securities and Exchange Commission (the “Commission” or the “SEC”) with respect to the Commission’s proposed rulemaking relating to credit ratings, Release No. 33-9186; 34-63874; File No. S7-18-08 (the “Proposing Release”).¹ We believe the Commission’s proposed rulemaking in this area is of significant consequence, and we respectfully submit this letter reflecting our comments.

The Proposing Release contains proposed rule and form amendments under the Securities Act of 1933 (the “1933 Act”) and the Securities Exchange Act of 1934 (the “1934 Act”). These amendments generally respond to the requirements of Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”).² In particular, Section 939A of the Dodd-Frank Act requires federal agencies to review “any regulation . . . that requires the use of an assessment of the credit-worthiness of a security . . .” and to “modify any such regulations . . . to remove any reference to or requirement of reliance on credit ratings and to substitute in such regulations such standard of credit-worthiness as each respective agency shall determine as appropriate for such regulations.” Section 939A also requires federal agencies “to establish to the extent feasible, uniform standards of credit-worthiness for use by each such agency. . . .”

Under the changes proposed in the Proposing Release, the eligibility requirements for the filing of registration statements on Forms S-3 and F-3 would be amended to eliminate currently

¹ 76 Fed. Reg. 8946 (February 16, 2011).

² Dodd-Frank Act, Pub. L. No. 111-203, 124 Stat. 1376, 1897 (July 21, 2010).



available criteria based on credit ratings and replace such criteria with an alternative test. Forms S-4 and F-4, and Schedule 14A, would be modified correspondingly. Certain rules under the 1933 Act, including Rules 138 and 139, would be modified in a parallel manner, and Rule 134 would be revised to remove the reference to credit ratings now contained in Rule 134(a)(17).

We believe the Commission took important steps when it adopted the Securities Offering Reform rules in 2005, and that those rules broadly encouraged registration of securities offerings by issuers and the appropriate dissemination of information to the marketplace. Through its rulemaking, the Commission has enhanced the ability of many seasoned issuers to access the public debt markets with greater speed and efficiency, and to take advantage of market opportunities as they arise. In considering any modification to the Form S-3 and F-3 eligibility rules, and to the safe harbors of Rules 134, 138 and 139, we believe it is very important to avoid changes that would discourage registration or diminish the availability of relevant information to market participants. There is a risk that the changes contained in the Proposing Release would force at least some seasoned issuers to conduct debt offerings under Rule 144A that would otherwise be registered on Form S-3 or F-3, particularly if such issuers are deprived of the speed and flexibility of shelf registration on those Forms. Furthermore, in considering modifications to Rules 134, 138 and 139, we believe it is important to avoid changes that would diminish the usefulness of those rules and thereby lead to a reduction in the availability of timely and relevant information, including securities research, in the marketplace. Our comments below are made with a view toward mitigating these potential consequences of the proposed rules.

I. Comments Responding to Similar Amendments Proposed by the SEC in 2008

Before turning to our comments on the Proposing Release, we would like to note that in 2008 the Commission proposed similar rule and form amendments. SIFMA's Credit Rating Agency Task Force commented on those proposed rule changes at the time.³ In its comment letter of December 8, 2009, SIFMA did not support elimination or replacement of credit ratings as eligibility criteria for purposes of Forms S-3 and F-3, nor did it support other changes related to credit ratings as then proposed. We believed at the time and we continue to believe that the use of credit ratings criteria in Forms S-3, F-3, S-4 and F-4 do not result in an excessive reliance on credit ratings by the Commission for regulatory purposes, nor do we believe they create any real risk of undue or inappropriate reliance by investors or other members of the public.

However, at the time of the Commission's 2008 proposals, the Dodd-Frank Act had not been enacted and the requirements of Section 939A did not apply. SIFMA recognizes that

³ See letter from SIFMA dated September 4, 2008 commenting on Release Nos. 33-8940 and 34-58071 ("SIFMA I") and letter from SIFMA dated December 8, 2009 commenting on Release Nos. 33-9069 and 34-60790, IA-2932 and IC-28940 ("SIFMA II").



Section 939A now mandates that the Commission take steps to remove credit ratings as a requirement in its regulations to the extent such regulations require the use of an assessment of credit-worthiness, and to adopt alternative standards the Commission determines to be appropriate. In our comments below, we therefore address substantively the changes contemplated by the Proposing Release and argue in favor of them in part and in favor of certain modifications in part. Our purpose is to minimize the adverse consequences to issuers, investors and markets that we believe may be occasioned by an undifferentiated implementation of the broad parameters of Section 939A, the purpose of which is not uniformly served by eliminating credit ratings entirely from every regulation in which reference to them appears. We argue, for that reason, that the Commission would be acting within its authority if it were to conclude, particularly in respect of references to credit ratings in certain safe harbor rules that the Commission proposes to modify, that Section 939A does not require removal of all references to ratings that appear in the SEC's regulations. In particular, we note that Section 939A obligated the Commission to review and modify only such regulations as “*require* the use of an assessment of the credit-worthiness of a security or money market instrument” (emphasis added), and we do not believe the permissive safe harbor provisions of Rules 134, 138 and 139, in particular, should be viewed as requiring the use of credit ratings.

II. Form S-3 and F-3 Eligibility Tests Based on the Amount of Non-Convertible Securities Issued within a Three-Year Period

The Commission proposes to replace the current investment-grade credit ratings criteria for eligibility for the use of Forms S-3 and F-3 with a test modeled on that used for the determination of WKSI eligibility. The test is based on an issuer having issued at least \$1 billion of non-convertible securities, other than common equity, in registered primary offerings for cash, not exchange, within the previous three years. Calculation of the amount of non-convertible securities issued would be done in a manner consistent with the WKSI test.

When the Commission first adopted the various criteria for eligibility to use short-form and shelf registration, it looked to tests, including the credit-ratings test, that it believed correlated well with how widely followed or well-known an issuer was in the debt markets.⁴ It does not appear that the Commission was focused primarily on creditworthiness.⁵ As the Commission said in its release adopting the S-3 eligibility rules, the Commission “made a concerted effort to revise the eligibility requirements in a manner . . . consistent with its intention

⁴ See Reproposal of Comprehensive Revision to System for Registration of Securities Offerings, Securities Exchange Release No. 33-6331 (Aug. 6, 1981), 46 Fed. Reg. 41,902 (Aug. 18, 1981) (the “S-3 Proposing Release”).

⁵ *Id.*, 46 Fed. Reg. at 41,904 (“[T]he proposed framework markedly reduces or eliminates those criteria relating to the “quality” of the registrant, and premises eligibility generally on dissemination of information in the market place.”).



to classify registrants on the basis of the degree of information disseminated and analyzed in the marketplace.”⁶ The Commission concluded that “[i]n addition to considering indicia of the quality of the registrant, security ratings are also based on marketplace information about the registrant which is analogous to the efficient market for widely followed equity securities.”⁷

The Commission considered but rejected other criteria when adopting the original Form S-3 eligibility rules, including earnings, market capitalization, number of shareholders, number of market makers, asset size and revenues.⁸ It regarded these as either insufficiently related to breadth of information dissemination in the market or so statistically related to public float as to be duplicative with the \$75 million public equity float test included in the proposed rules. In now proposing to amend the short-form and shelf-eligibility rules to eliminate any credit ratings test, the Commission has properly looked to identify a substitute measure correlated to an issuer’s breadth of following in the market and dissemination of information among investors, rather than a measure more overtly tied to perceived credit quality.

SIFMA generally believes that a test for Form S-3 and F-3 eligibility based on an issuer having issued \$1 billion of non-convertible securities within the last three years is reasonable, because we concur with the Commission that it will generally correlate well with issuers that are well-known and widely followed in the market. However, it is our view that the new Form S-3 and F-3 eligibility rules need not match the WKSI eligibility rule precisely, nor is it appropriate for them to be as stringent. We do not believe that Section 939A’s mandate to adopt “uniform standards of creditworthiness” should be construed to imply that the new Form S-3 and F-3 eligibility tests must be conformed to the WKSI test (or any other existing regulatory standard). In particular, we note that WKSI eligibility triggers results under other rules (including, for example, automatic effectiveness of registration statements, use of free-writing prospectuses and the permissible timing of offers of securities by issuers)⁹ that reasonably should apply to a narrower universe of registrants than should eligibility to use short-form and shelf registration.

In addition, we strongly believe the Commission should be careful not to unnecessarily exclude from Form S-3 and F-3 eligibility issuers that have enjoyed short-form and shelf access to the public capital markets in the past. This is particularly important because it has not been shown by the Commission or Congress that such issuers, having relied on the investment grade credit ratings criterion to file registration statements under Forms S-3 or F-3, have represented

⁶ *Id.* at 41,905.

⁷ *Id.* at 41,910.

⁸ *Id.* at 41,907.

⁹ Securities Act of 1933 Rule 163 [17 C.F.R. 230.163]. Form S-3 General Instruction I.D allows WKSI shelf registration statements on S-3 and F-3 to be automatically effective upon filing.



any particular risk to investors or the market or caused any undue reliance by investors on credit ratings. Moreover, we believe there is a substantial likelihood that many issuers would choose to migrate their financing activities to the Rule 144A or Regulation S markets, rather than register their securities on Forms S-1 or F-1, in order to maintain the speed to market and timing flexibility on which they have come to rely.

We would therefore urge the Commission to modify its present proposal in the following specific ways:

1. Include Rule 144A offerings of non-convertible securities. In calculating whether an issuer has issued \$1 billion of non-convertible securities within the previous three years, we believe issuers should be permitted to count securities issued for cash pursuant to Rule 144A. Such debt issuances contribute materially to the degree to which institutional investors follow issuers and the degree to which professional analyses and other information regarding such issuers is disseminated in the marketplace. Inclusion of Rule 144A non-convertible securities will enable widely followed issuers of substantial issuance volume to reach and maintain eligibility to use short-form registration and, we believe, will increase rather than decrease the likelihood that they will undertake registration of their debt securities for purposes of future issuances. As noted above, we believe many issuers that lose the ability to use Form S-3 or F-3 will likely opt to use Rule 144A offerings, rather than file Form S-1 or F-1 registration statements. Without including Rule 144A securities, these issuers would perpetually be excluded from short-form and shelf registration eligibility because they will be forced to rely again and again on unregistered offerings for their financing needs.
2. Include non-convertible securities issued in registered exchange offers. Securities issued in registered exchange offers should not be excluded, except (in order to avoid double-counting) exchange offers for securities that were previously issued under Rule 144A within the same three-year period and which are permitted to be included in the calculation of eligibility as described in the preceding paragraph. We believe that exchange offer securities contribute meaningfully to the degree to which issuers are widely followed in the marketplace, particularly among institutional holders and professional analysts. Moreover, permitting the inclusion of exchange offer securities would help mitigate the potential for the new rule to be under-inclusive and lead to a loss of eligibility among seasoned issuers previously entitled to use short-form registration.
3. Include U.S. dollar-denominated securities sold offshore under Regulation S as part of an offering also eligible to be sold to U.S. investors pursuant to Rule 144A. In conjunction with allowing Rule 144A-eligible non-convertible securities to be

included for purposes of the eligibility test proposed by the Commission, we believe it is necessary and appropriate to also include securities that are part of the same offering but which may be sold offshore pursuant to Regulation S, at least insofar as such securities are U.S. dollar-denominated. First, such debt often trades permissibly into the U.S. market after the requisite seasoning period and thereby contributes to the trading and following an issuer's debt enjoys among U.S. investors. Second, markets are increasingly global, information is disseminated across and among markets, particularly for U.S. dollar-denominated debt, and an issuer's wide market following outside the United States contributes to its following in the United States. Third, and perhaps most problematically, exclusion of Regulation S securities from the eligibility test will lead to difficulties in calculating eligibility if securities issued pursuant to Rule 144A are permitted to be counted. This is because issuers often make offers and sales of their securities to both U.S. investors, under Rule 144A, and non-U.S. investors, in reliance on Regulation S, as part of the same primary offering. Disaggregating such Regulation S sales, and not permitting the full aggregate amount initially issued at the time of its issuance to be counted, will lead to substantial, and we think unwarranted, complexity, together with a potential for uncertainty or error in the calculation by issuers and others of a company's eligibility under the new rule.¹⁰

4. The Commission should also consider providing a parallel eligibility test based on total debt outstanding at the time of filing a registration statement on Form S-3 or F-3. We believe that in addition to the test we propose based on at least \$1 billion of registered and Rule 144A/Regulation S debt issued (for cash or exchange) during the previous three years, it would be appropriate, and could be very helpful to issuers, to also permit eligibility based on an issuer having \$1 billion of debt (other than commercial paper or other debt with original maturities of less than one year) outstanding at the time of the filing of its registration statement of Form S-3 or F-3. Consistent with our proposals above, such currently outstanding debt should be permitted to include debt issued in registered or Rule 144A primary offerings for cash, debt issued in registered exchange offers (without double-counting), and U.S. dollar-denominated debt issued offshore. We would not propose this as a substitute

¹⁰ If the inclusion of such dollar-denominated securities is viewed by the Commission as unacceptable, an alternative to be considered would be the inclusion of all non-convertible securities issued for cash pursuant to Rule 144A and Regulation S at such time as a registered exchange offer is conducted in respect of such securities (i.e., a so-called Exxon Capital exchange offer). We believe this approach is inferior to the approach we suggest, in part because it permanently excludes from the calculation any debt issued under Rule 144A that is not subject to a registered exchange after issuance (e.g., so-called "Rule 144A for life" securities). However, such an approach would be better than limiting the calculation exclusively to securities issued in registered primary offerings for cash, not exchange, as contemplated by the Proposing Release.

for the amount-issued test, but rather an additional way in which issuers could achieve eligibility.¹¹ Issuers in certain industries may issue in substantial volume, but with irregular timing and frequency. In any particular three-year period, some issuers may not issue \$1 billion in aggregate debt, while in other three-year periods they may. However, such issuers, if they have substantial outstanding debt, remain widely followed by investors. An additional eligibility criterion based on such a measure would appropriately give them the benefit of shelf registration and, importantly, help lessen the degree to which eligibility for certain issuers would vary over time depending on their frequency of issuance without any real change in their market following or other circumstances.

III. Form S-3 and F-3 Eligibility Test Based on Status as a Subsidiary of a Form S-3 or F-3 Eligible Company

As the Commission notes in the Proposing Release, there is a risk in the new eligibility requirements that seasoned issuers that have enjoyed short-form and shelf registration eligibility for many years will be excluded.¹² The Commission noted in the Proposing Release that it had identified an estimated 45 issuers previously eligible to use Form S-3 (and that had made a registered offering during the period from January 1, 2006 to August 15, 2008) that would lose their eligibility under the proposed criteria.¹³ We suspect this count may underestimate the actual number of previously eligible issuers that would lose their eligibility under the Commission's proposal. We reviewed available information for companies in the electric utility sector that we could determine had issued debt during the period March 2008 to March 2011, and we calculated the amount of non-convertible securities, other than common stock, issued by each of them in public offerings during that three-year period. Our survey identified approximately 120 such issuers in total. Of the total, approximately 90 appeared to have issued less than \$1 billion of such debt. Of those, we believe approximately two-thirds (at least 60) are operating company subsidiaries that would not meet the \$75 million public float test of Form S-3 and likely are relying on the investment grade ratings test for their Form S-3 eligibility.¹⁴

¹¹ Just as Forms S-3 and F-3 currently provide multiple Transaction Requirements which can be met in order for an issuer to use such Forms, so too can the amended versions of such Forms.

¹² Proposing Release, 76 Fed. Reg. 8946, 8950.

¹³ *Id.*

¹⁴ In our review of these issuers, we endeavored to exclude those whose securities were issued with a parent guarantee and therefore may be relying on General Instruction I.C of Form S-3, rather than the investment grade ratings test, for their eligibility. We relied on data available via Bloomberg for our identification of utility sector issuers that had issued public debt during the three-year period from March 2008 to March 2011.



In our view, there is no substantive reason to narrow the universe of publicly reporting companies, already widely followed in the market, that receive the benefits of Form S-3 or F-3 eligibility. The benefits to such companies are substantial, and include the ability to raise capital efficiently, in prompt response to market opportunities, and to manage their financing plans with flexibility through periodic shelf takedowns and other delayed or continuous offerings. We recognize that it may not be possible to change the shelf eligibility rules in a manner consistent with Section 939A of Dodd-Frank without altering somewhat the roster of companies eligible at any given time to use Forms S-3 and F-3. Nonetheless, we believe strongly that every effort should be made by the Commission to avoid having the adverse effects of the new rule fall disproportionately and unfairly on any one category of issuer.

We note that when similar rule changes were proposed by the Commission in 2008, several commenters expressed the view that the changes would most adversely affect state-regulated electric utilities, exchange-listed REITs, finance companies and perhaps other categories of companies that tend to finance their operations through issuances of securities by their wholly owned operating company subsidiaries.¹⁵ Our survey of recent issuers described above supports this view. These subsidiary issuers are 1934 Act reporting companies,¹⁶ but as wholly owned subsidiaries they do not meet the public float test for Form S-3 or F-3 eligibility. Some of their parent companies have multiple operating company subsidiaries utilizing shelf registration in regularly accessing the public debt markets, but these sister subsidiaries may differ in the amount and frequency of their debt issuances. Some may issue \$1 billion of debt within three years, while many others do not. In many cases, securities issued by such operating companies do not carry a parent guarantee, and such a guarantee is not necessary for their

¹⁵ See, e.g., letter from Edison Electric Institute dated September 5, 2008 commenting on SEC Release Nos. 33-8940 and 34-58071 (noting that at least 25 to 30 electric utilities would be negatively affected); letter from Wisconsin Energy Corporation dated September 5, 2008 commenting on Release No. 33-8940 (stating that if the rule changes set forth in the Release were adopted, its utility subsidiary would become ineligible for Form S-3 because it only issued \$300 million in debt securities over the last three years); letter from American Electric Power dated September 4, 2008 commenting on Release No. 33-8940 (noting that five of its six utility subsidiaries would become ineligible if the proposed rule was adopted); letter from National Association of Real Estate Investment Trusts dated September 5, 2008 commenting on Release No. 33-8940 (stating that under the terms of the Proposal the vast majority of REITs would in practice be precluded from accessing public debt capital markets through use by their operating partnership subsidiaries of the short-form shelf-registration process).

¹⁶ Such issuers are typically eligible to use Form S-3 pursuant to General Instruction I.C.2 of Form S-3, because their parents meet the registrant test and the subsidiary is engaged in a primary offering of non-convertible investment grade securities. In order to use Form S-3, such companies must also file periodic reports pursuant to Section 13(a) or 15(d) of the 1934 Act so as to comply with Item 12 of Part I of Form S-3, which requires the incorporation by reference in the registration statement of certain reports. Therefore, even if such companies are wholly owned subsidiaries, they will be 1934 Act reporting companies, typically by having registered their equity securities under Section 12(g) of the 1934 Act.



securities to be marketable or to be widely followed in the marketplace. Operating company subsidiary issuers owned by a common parent are often invested in, and professionally followed, by the same institutional holders and professional analysts that follow the parent company. They are widely followed in the marketplace, on their own and in conjunction with their parent entities. In many cases, they are also followed in conjunction with other reporting-company subsidiaries of the same parent that operate in adjacent markets within the same industry (e.g., electric utilities).

In light of this, and to ensure that the Commission's proposed rule change does not fall disproportionately and unfairly on these operating company subsidiary issuers, we would propose the following:

1. Issuers that are direct or indirect majority-owned subsidiaries should be eligible to use Form S-3 or F-3 if the parent meets the registrant requirements and the parent, the issuer subsidiary and other majority-owned subsidiaries of the parent collectively have issued \$1 billion of non-convertible securities within the previous three years. In recognition of the established practice in certain industries of financing operations at the operating company subsidiary level, and the existence in some cases of multiple operating subsidiary issuers under one corporate parent, we urge the Commission to permit companies to count the total non-convertible debt securities issued (other than commercial paper or other debt with original maturities of less than one year), during the previous three years, not only by the issuer subsidiary but also by the parent and all other direct and indirect majority owned subsidiaries that, with such calculation, could use Form S-3 or F-3. This would recognize the fact that such groups of affiliated operating companies, under a single parent, are widely followed in the marketplace with sufficient and comparable dissemination of information among investors. As such, giving them uniform access to Form S-3 or F-3 registration would be appropriate and would avoid disparate treatment of otherwise comparably situated corporate entities within the same family. We do not believe that there would be any interest served by requiring each such subsidiary separately to meet an eligibility test based on having issued, within three years, \$1 billion of non-convertible securities, and doing so would render ineligible many currently eligible operating subsidiaries while other subsidiaries of the same parent may retain their eligibility. Consistent with our proposals above, non-convertible securities permitted to be counted should include debt issued in registered or Rule 144A primary offerings for cash, debt issued in registered exchange offers (without double counting), and U.S. dollar-denominated debt issued offshore. Based on our survey of recent issuers described above, we believe a majority of the operating company subsidiary issuers we identified as at risk of losing their shelf eligibility under the proposed rules would retain their eligibility under the test we suggest here.

2. As an alternative, or in addition, to the test described in the preceding paragraph, a wholly-owned subsidiary could be allowed eligibility to use Form S-3 or F-3 if its ultimate parent meets both the registrant requirements and applicable transaction requirements of the Form.¹⁷ This would be similar to eligibility currently permitted under General Instruction I.C.3 to Form S-3 and General Instruction I.A.5 of Form F-3 but would be provided only to direct or indirect wholly owned (as opposed to majority-owned) subsidiaries and would not be required to carry the guarantee of the parent. Such a rule would recognize that wholly owned subsidiaries of the type now utilizing Form S-3 or F-3 (in reliance on the investment grade rating criteria) are typically traded, analyzed and followed by the market in very close conjunction with their parents. We would argue that a parent guarantee of securities should not be required in order for such wholly owned subsidiaries to get the benefits of Form S-3 or F-3 eligibility. We note, for example, that wholly owned subsidiaries are already accorded the benefit of limited disclosure in their 1934 Act periodic reports in reliance on their parents' filing of full reports, and this is not conditioned on the presence of a parent company guarantee (nor on any credit rating criteria).¹⁸ We believe that it would be reasonable for the Commission to consider creating a new Form S-3 and F-3 eligibility standard for wholly owned subsidiaries, similar to the one currently available to majority-owned subsidiaries, but without requiring a parent guarantee.¹⁹

IV. Grandfathering of Currently Eligible Issuers

In SIFMA's comments to similar Form S-3 and F-3 eligibility amendments proposed by the Commission in 2008, we indicated that currently eligible issuers should be permitted to continue to use Forms S-3 and F-3 for a period of at least two years from any final rule

¹⁷ The parent company could meet the transaction requirements of the Form in this case by meeting either the \$75 million public float test or the test requiring issuance of at least \$1 billion of non-convertible securities within the previous three years (using the definition of includable securities we have proposed in this letter).

¹⁸ See Form 10-K General Instruction I; Form 10-Q General Instruction H.

¹⁹ We also believe that it could be reasonable for the Commission to consider a more fundamental revision of the rules governing Form S-3 and F-3 eligibility that would involve eliminating altogether the current transaction requirements, and, effectively, permit companies the benefits of short-form and shelf eligibility if they have been reliably filing reports under the 1934 Act for at least one year. Such a rule change would reflect a recognition of the technological changes in information dissemination and the increased rigor of disclosure rules in recent years. For example, company reports now are immediately accessible via EDGAR and the Internet, the reporting requirements under Form 8-K have been made more rigorous and timely, and Regulation FD has reduced the risk of selective disclosure.



amendment, without regard to such issuer's eligibility under the new rules.²⁰ We continue to believe that a grandfathering period is warranted and would help ensure that companies have sufficient time to adjust to the new eligibility standards and to plan their capital-raising activities efficiently without undue cost or burden. In the context of the Commission's currently proposed rule and form amendments, we would now propose that a grandfathering clause be adopted to permit any currently eligible issuer to retain its eligibility until the later of (i) two years from the effective date of the new rules and (ii) the latest expiration date of a registration statement on Form S-3 or F-3 that is effective as of the effective date of the new rules.²¹ We do not believe that Section 939A of Dodd-Frank should be construed against the implementation of any reasonable grandfathering period, either with respect to the proposed changes to Form S-3 and F-3 eligibility or any other rule change the Commission may undertake in response to Section 939A.

V. Other Potential Eligibility Criteria Mentioned in the Proposing Release²²

Without addressing each in detail, we believe that while the test proposed by the Commission based on aggregate amount of debt issued is usefully correlated to how well-known and widely followed an issuer is, some of the alternative tests on which the Commission asked for comments would be more problematic in their effect or implementation.

For example, market-related factors are harder to measure and would be less reliable indicators of how widely followed an issuer is. We believe that average daily trading volume is an imperfect barometer, as the debt securities of some large, well-followed issuers may not trade actively day to day. The total number of beneficial owners of an issuer's debt securities may be hard to assess accurately and easily, while record ownership (given that DTC is frequently the only record holder) would be an imperfect gauge of how widely held an issuer's securities are. Other tests that might arguably better address the question of an issuer's perceived creditworthiness may not be relevant to how widely followed an issuer is or how well-disseminated issuer-related information is. Moreover, most measures of perceived creditworthiness that do not involve credit ratings are likely to be much more market dependent and exhibit volatility that is extrinsic to the condition of the issuer. For example, market

²⁰ SIFMA I, at 15 (September 4, 2008).

²¹ If the Commission were concerned that such a grandfathering clause would create an undesirable incentive for issuers to file registration statements after adoption but before effectiveness of the rule changes, merely in order to get the benefit of grandfathering, clause (ii) of this sentence could be modified to refer to the latest expiration date of a registration statement on Form S-3 or F-3 that is effective as of the effective date of the new rules *and was filed prior to the date of adoption by the Commission of such rules*. We believe adoption of our other various proposals in this letter would also greatly mitigate any such incentive.

²² Proposing Release, 76 Fed. Reg. at 8952.



observers often look at the yields at which an issuer's debt securities trade in relation to U.S. Treasuries of like maturities (generally referred to as Treasury spreads). Treasury spreads change with changes in an issuer's perceived creditworthiness; however, they also change in relation to broader market changes, movements in interest rates and other extrinsic factors (including general economic or industry conditions). It would be difficult to implement a rule-based eligibility criterion that relied on Treasury spreads because of how changeable such spreads tend to be over time.

We also believe that criteria based on company-specific financial tests would likely be imperfect, at best, as companies differ materially in these respects even among those with similar market and credit characteristics. We note that the SEC moved away from such measures when it originally adopted Forms S-3 and F-3, electing to use credit ratings as a criterion.²³ As the Commission notes in the Proposing Release, such earlier criteria related to company-specific measures of net income, the absence of defaults and the existence of various fixed charge coverages.²⁴ We do not believe that any such measure, or any similar measure that might involve net capital levels, revenues or profitability, other financial ratios, returns on assets, or the presence or absence of certain debt covenants would be sufficiently uniform in its relevance or applicability among issuers to be useful for purposes of a Form S-3 and F-3 eligibility rule.

VI. Risk that the Proposed Form S-3 and F-3 Eligibility Tests will be Over-Inclusive

In its Proposing Release, the Commission asks whether the proposed rule and form amendments risk extending eligibility to issuers for whom it is not appropriate.²⁵ We do not believe that this would be the consequence of either the changes as proposed in the Proposing Release or such changes as modified by our proposals in this letter. Non-investment grade issuers can already use Forms S-3 and F-3 by meeting the registrant test and having a public float of at least \$75 million. We note the very significant growth of the non-investment grade debt markets since the adoption of Forms S-3 and F-3, and we believe that issuers of such debt are much more widely followed today. There will likely be a limited number of formerly ineligible issuers that would come to have Form S-3 or F-3 eligibility under the new rules because, while they do not meet the \$75 million public float test, they would meet a new issued debt test. Some of these may issue non-investment grade rated securities. We believe such issuers will be widely followed in the market, with an established 1934 Act reporting history, similar to that of many non-investment grade issuers currently using Form S-3 or F-3. We therefore do not consider

²³ S-3 Proposing Release, 46 Fed. Reg. at 41,910 ("Rather than base the availability of Form S-3 on specified quality of the issuer criteria, the Commission believes that security ratings are a more appropriate standard.").

²⁴ Proposing Release, 76 Fed. Reg. at 8947 n.27.

²⁵ *Id.* at 8949.



their potential eligibility to register securities on Form S-3 or F-3 to be at all problematic. Moreover, some issuers falling in this category will be drawn to the greater certainty and efficiency of short-form registration for their debt issuances where they previously would have issued such debt in reliance on Rule 144A or another exemption. We believe migration by such issuers to registered offerings would generally advance investor protection goals, and would be consistent with the Commission's broad policy preference for registered offerings.

VII. Proposed Changes to Rule 134(a)(17)

SIFMA urges the Commission not to amend Rule 134 in the manner contemplated by the Proposing Release. We believe that the reference to credit ratings in Rule 134(a)(17) remains appropriate and is very helpful to issuers and investors alike. We do not believe that Section 939A of Dodd-Frank should be read to require the deletion of a reference to credit ratings where, as in Rule 134(a)(17), it appears within a safe harbor rule as part of a list of allowable, but not required, information. As noted above, Section 939A mandates modification only of regulations that "require the use of an assessment of credit-worthiness of a security," and we do not believe Rule 134(a)(17) should be regarded as such. The safe harbor of Rule 134 allows an offering participant to disseminate objective factual information widely regarded as relevant by investors without incurring undue risk that such dissemination of information will be construed as violative of the prospectus rules under the 1933 Act. In including credit ratings among such permitted information, we do not believe the rule endorses, or encourages any reliance on, credit ratings. Rather, the rule properly reflects the fact that credit ratings are normally relevant to investors and others who follow issuers, that they are part of the mix of information generally available to the market, and that reference to them in an otherwise limited communication should not alter the legal characterization of such communication. Moreover, elimination of the reference to credit ratings in the safe harbor of Rule 134 could have the unintended, and less desirable, result of increasing references to credit ratings in other materials, including free writing prospectuses. This could give such information heightened, rather than reduced, prominence to the extent included in free writing prospectuses, while disadvantaging certain categories of issuers that are not able to use free-writing prospectuses, but which otherwise have a legitimate interest in disseminating ratings information to the market. Among such issuers are many business development companies, SPACs, closed-end funds and other companies registered under the Investment Company Act of 1940.

VIII. Proposed Changes to Rules 138 and 139

For similar and additional reasons, SIFMA urges the Commission not to amend Rules 138 and 139 to eliminate references to investment grade credit ratings. Again, we do not believe Section 939A of Dodd-Frank should be read to require removal of references to credit ratings in the context of safe harbor rules intended to provide greater certainty in avoiding the risk of an unintended securities law violation. Moreover, elimination of the references to credit ratings in



Rules 138 and 139 will place a substantial and unwarranted additional burden and liability risk on securities firms that publish securities research and on the research analysts, supervisory analysts and research compliance professionals at such firms.

Under current practice, research analysts, supervisory analysts and the relevant compliance functions are able to determine quickly and assuredly whether a particular research publication is entitled to the safe harbor protection of Rule 138 or 139 by virtue of the published credit rating of the subject company. In many cases, the timeliness of the release of research publications is of substantial importance to investors. Timely release of research views is beneficial to the market and the overall objective of broad dissemination of information on widely followed issuers. Under the Commission's proposed changes to Rules 138 and 139, there is a substantial risk that research analysts and their supervisors could not practically avail themselves of either safe harbor, as they would now need to assess Form S-3 or F-3 eligibility on the basis of their calculation of the amount of debt issued by the subject company over a rolling three-year time period. To conclude that the safe harbor of Rule 138 or 139 were available, they would have to be highly confident in their ability accurately to calculate aggregate debt issuances over time for each subject company, and to do so with sufficient objective certainty to eliminate the risk to their firms of an error in calculation or reliance on inaccurate or incomplete data. Moreover, they would have to be able to complete such analysis quickly in order to allow research to be published in timely response to company and market developments, as it is today. Any miscalculation could lead to a determination after the research has been published that the safe harbor of the rules is not available. This could have serious consequences to the research-writing firm, the subject company and any securities offering that may be pending. In addition to potential liability for a regulatory violation, the firm may be precluded from participating in such an offering as an underwriter and the offering itself may be delayed or complicated as a result.

We believe these factors argue strongly in favor of retaining the existing use of credit ratings for purposes of the Rule 138 and 139 safe harbors. No policy objective of Section 939A would seem to be served by its elimination, and the negative effect on the publication of research could be material. We believe the proposed change, if adopted, would adversely affect the publication of research analyses in timely response to market and company developments. The complexity, and therefore the risk, to securities firms for their determinations regarding the availability of the safe harbors will be substantially increased. In the presence of doubt as to the availability of the safe harbor, research analysts and compliance professionals may be expected to refrain from publishing or delay release of research notes and reports, to the detriment of investors and markets.



IX. Proposed Changes to Forms S-4 and F-4 and Schedule 14A

The Commission proposes to amend Forms S-4 and F-4 and Schedule 14A so as to correspond with and incorporate parallel changes to the eligibility criteria for Forms S-3 and F-3. We support such changes, with the modifications and additions to the Forms S-3 and F-3 eligibility criteria we propose above.

X. Conforming Change to FINRA Rule 5110

FINRA Rule 5110²⁶ (the Corporate Financing Rule), which was adopted by FINRA pursuant to authority delegated to it by Congress and the SEC and approved by the SEC, prohibits FINRA members (and associated persons) from participating in certain public offerings unless documents required by the rules have been filed with, and reviewed by, FINRA. Certain offerings are exempted from this filing requirement, including: (i) securities (other than equity issued in an IPO) of an issuer that has outstanding at time of issuance non-convertible debt or preferred stock rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories (Rule 5110(b)(7)(A)); (ii) offerings of non-convertible debt or preferred stock rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories (Rule 5110(b)(7)(B)); (iii) offerings of securities registered with the SEC on Form S-3 or F-3 pursuant to the standards for those Forms prior to October 21, 1992 and offered pursuant to Rule 415 of Regulation C (Rule 5110(b)(7)(C)(i)); (iv) financing instrument-backed securities that are rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories (Rule 5110(b)(7)(E)); and (v) exchange offers of securities issued by a company that is eligible to register securities on Forms S-3 or F-3 pursuant to the standards for those Forms prior to October 21, 1992 (Rule 5110(b)(7)(F)(ii)). Each of these exclusions contains references to credit ratings, either explicitly or indirectly by reference to Form S-3 and F-3 eligibility standards as in effect on October 21, 1992.²⁷

²⁶ See FINRA Rule 5110, available at http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=6831.

²⁷ We recognize that Section 939A refers to regulations “issued by” a federal agency. FINRA rules technically are issued by a self-regulatory organization that is not a federal regulatory agency. However, all FINRA rules must be approved by the Commission, and FINRA operates pursuant to authority delegated to it by Congress and the Commission, so we believe it is possible that Congress could conclude that FINRA rules are in fact subject to Section 939A, although we are expressing no view on such a position.



We recommend that Rule 5110 be amended promptly to conform the exclusions noted above to the changes to Form S-3 and F-3 eligibility that the Commission adopts in response to Section 939A of the Dodd-Frank Act.²⁸ We believe that failure to do so will create unnecessary complexity and cost for certain capital markets transactions, with no appreciable corresponding investor protection benefit. We therefore urge the SEC to work with FINRA to amend Rule 5110 as soon as possible.

XI. Conclusion

We very much appreciate your consideration of the views expressed in this letter. We believe that the Proposing Release contains a number of ideas that are helpful and practical in light of the changes to Form S-3 and F-3 eligibility that the Commission has determined it must undertake under Section 939A of the Dodd-Frank Act. However, we urge the Commission to use its discretion under Section 939A to refrain from a wholesale elimination of references to credit ratings in certain rules, such as safe harbor rules, where Section 939A would not appear to require a change, its purpose would not be served by such a change, and the result will be to reduce, rather than increase, the availability of useful information in the marketplace. Furthermore, we urge the Commission to consider our specific proposals above for expanding the eligibility criteria for Forms S-3 and F-3 beyond those criteria proposed by the Commission in the Proposing Release. We believe our suggestions are consistent with and further the Commission's overall objectives, including by mitigating the impact of the rule changes on issuers currently entitled to use Forms S-3 and F-3, encouraging rather than discouraging registration and ensuring that short-form and shelf registration eligibility is properly focused on those reporting companies that are widely followed by investors in the marketplace.

²⁸ We note that Rule 5110's reliance on Form S-3/F-3 eligibility as of October 21, 1992 has resulted in Rule 5110's exclusions no longer aligning with current shelf registration practice. In particular, a subset of WKSIs are not eligible to avail themselves of the shelf registration statement exclusion from Rule 5110. Subsequent to the adoption of Securities Offering Reform, FINRA proposed to amend Rule 5110 to exempt all offerings by WKSIs from the filing requirement of Rule 5110, but that rule proposal was withdrawn in 2009 (Form 19b-4 relating to File No. SR 2004-022 (August 5, 2009)). While such proposed rule change was pending, FINRA undertook to review and respond to Rule 5110 filings by WKSIs that were ineligible for the shelf registration exemption on an expedited basis to minimize disruption to offerings by such issuers.



We thank the Commission for the opportunity to comment in advance of its rulemaking in this area. Should you have any questions regarding our comments, please do not hesitate to contact the undersigned at 212-313-1118 or Frederick J. Knecht of Covington & Burling LLP at 212-841-1193.

Sincerely yours,

A handwritten signature in dark ink, reading "Sean Davy". The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

Sean Davy
Securities Industry and Financial Markets Association

cc: Robert Cook, Director, Division of Trading and Markets
Meredith Cross, Director, Division of Corporation Finance
Eileen Rominger, Director, Division of Investment Management