Wednesday,
November 22, 2006

Part IV

Securities and Exchange Commission

17 CFR Part 230
Covered Securities Pursuant to Section 18 of the Securities Act of 1933; Proposed Rule
Covered Securities Pursuant to Section 18 of the Securities Act of 1933

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission ("SEC" or "Commission") proposes for comment an amendment to a Rule under Section 18 of the Securities Act of 1933 ("Securities Act"), as amended, to designate certain securities listed on The NASDAQ Stock Market LLC ("NASDAQ") as covered securities for purposes of Section 18 of the Securities Act. Covered securities under Section 18 of the Securities Act are exempt from state law registration requirements.

DATES: Comments should be received on or before December 22, 2006.

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments

• Use the Commission’s Internet comment form (http://www.sec.gov/rules/proposed.shtml); or

• Send an e-mail to rule-comments@sec.gov. Please include File Number S7–18–06 on the subject line; or

• Use the Federal eRulemaking Portal (http://www.regulations.gov). Follow the instructions for submitting comments.

Paper Comments

• Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–1000.

All submissions should refer to File Number S7–18–06. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments received by any method to http://www.sec.gov/rules/proposed.shtml. Comments are also available for public inspection and copying in the Commission’s Public Reference Room, 100 F Street, NE., Washington, DC 20549. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT:

Hoather Seidel, Senior Special Counsel, (202) 551–5608, Hong-anh Tran, Special Counsel, (202) 551–5637 or Michou Nguyen, Special Counsel, (202) 551–5634, Division of Market Regulation ("Division"), Commission, 100 F Street, NE., Washington, DC 20549–6628.

SUPPLEMENTARY INFORMATION:

I. Introduction

In 1996, Congress amended Section 18 of the Securities Act to exempt from state registration requirements securities listed, or authorized for listing, on the New York Stock Exchange LLC ("NYSE"), the American Stock Exchange LLC ("Amex"), or the National Market System of The NASDAQ Stock Market LLC ("NASDAQ/NGM") (collectively, the "Named Markets"), or any national securities exchange designated by the Commission to have substantially similar listing standards to those markets. More specifically, Section 18(a) of the Securities Act provides that "no law, rule, regulation, or order, or other administrative action of any State shall directly or indirectly apply to a security that—(A) is a covered security." Covered securities are defined in Section 18(b)(1) of the Securities Act to include those securities listed, or authorized for listing, on the Named Markets, or securities listed, or authorized for listing, on a national securities exchange (or tier or segment thereof) that has listing standards that the Commission determines by rule are "substantially similar" to the Named Markets. Pursuant to Section 18(b)(1)(B) of the Securities Act, the Commission adopted Rule 146(b) which lists those national securities exchanges, or segments or tiers thereof, that the Commission has determined to have listing standards substantially similar to those of the Named Markets and thus securities listed on such exchanges are deemed covered securities. Nasdaq has petitioned the Commission to amend Rule 146(b) to determine that its listing standards for securities listed on the Nasdaq Capital Market ("NCM") are substantially similar to those of the Named Markets and, accordingly, that securities listed pursuant to such listing standards are covered securities for purposes of Section 18(b) of the Securities Act. If the Commission makes this determination, then securities listed on the NCM would be exempt from state law registration requirements.

II. Background

In 1998, the Chicago Board Options Exchange, Incorporated ("CBOE"), Pacific Exchange, Inc. ("PCX") (now known as NYSE Arca, Inc.), the Philadelphia Stock Exchange, Inc. ("Phlx"), and the Chicago Stock Exchange ("CHX") petitioned the Commission to adopt a rule determining that specified portions of the exchanges’ listing standards were substantially similar to the listing standards of the Named Markets. In response to the petitions, and after extensive review of the petitioners’ listing standards, the Commission adopted Rule 146(b), determining that the listing standards of the CBOE, Tier 1 of the PCX, and Tier 1 of the Phlx were substantially similar to those of the Named Markets and that securities listed pursuant to those standards would be deemed covered securities for purposes of Section 18 of the Securities Act. Further, in 2004, the International Stock Exchange, Inc. ("ISE") petitioned the Commission to amend Rule 146(b) to determine that its listing standards for securities listed on ISE are substantially similar to those of the Named Markets and, accordingly,
that securities listed pursuant to such listing standards are covered securities for purposes of Section 18(b) of the Securities Act.\footnote{See letter from Michael Simon, Senior Vice President and General Counsel, ISE, to Jonathan G. Katz, Secretary, Commission, dated October 9, 2003.} The Commission subsequently amended Rule 146(b) to designate options listed on ISE as covered securities.\footnote{Securities Act Release No. 8442 (July 14, 2004), 69 FR 43295 (July 20, 2004).}

Nasdaq has petitioned the Commission to amend Rule 146(b) with a determination that its listing standards for securities listed on the NCM are substantially similar to those of the Named Markets, and that NCM securities are “covered securities” under Section 18(b) of the Securities Act.

### III. Discussion

Under Section 18(b)(1)(A) of the Securities Act, the Commission has the authority to compare the listing standards of a petitioner with those of either the NYSE, Amex, or Nasdaq/NGM. The Commission has compared Nasdaq’s listing standards for all NCM securities with only one of the Named Markets if the listing standards in a particular category did not meet the standards of that market, the Commission compared the standards to the other two markets.\footnote{15 U.S.C. 77r(b)(1)(A).} In addition, the Commission has interpreted the “substantially similar” standard to require listing standards at least as comprehensive as those of the Named Markets.\footnote{This approach is consistent with the approach that the Commission has previously taken. See Securities Act Release Nos. 7422 (June 9, 1997), 62 FR 32705 (June 17, 1997) and 7494 (January 13, 1998), 63 FR 3012 (January 21, 1998).} If a petitioner’s listing standards are higher than the Named Markets, then the Commission may still determine that the petitioner’s listing standards are substantially similar to the Named Markets. Finally, the Commission notes that differences in language or approach would not necessarily lead to a determination that the listing standards of the petitioner are not substantially similar to those of a Named Market.

The Commission has reviewed listing standards for securities traded on NCM\footnote{Securities Act Release No. 4320 (November 30, 2006), 71 FR 76088 (November 28, 2006).} and, for the reasons discussed below, preliminarily believes that the standards overall are not substantially similar to those of a Named Market. However, Nasdaq has filed a proposed rule change to amend its quantitative listing standards for NCM securities.\footnote{See generally Nasdaq Rules 4310, 4320, and 4350.}

In view of Nasdaq’s proposed rule change, the Commission preliminarily believes that it could make a finding that the NCM’s listing standards are substantially similar to those of a Named Market, and thus amend Rule 146(b) to include securities listed on the NCM. The Commission also notes that Nasdaq’s qualitative listing standards for NCM securities are identical to the qualitative listing standards for Nasdaq/NGM securities.\footnote{See generally Nasdaq Rules 4310(c)(2)(A)(ii), (iii), and 4310(c)(7)(A).}

#### A. Common Stock

As discussed below, the Commission preliminarily believes that some, but not all, of the requirements in Nasdaq’s quantitative initial listing standards for common stock listing on the NCM are substantially similar to those of Amex’s common stock listing standards. The Commission therefore preliminarily believes that the NCM common stock initial listing standards are not currently substantially similar to those of Amex’s common stock listing standards. Specifically the Commission preliminarily believes that the NCM listing requirements are substantially similar to Amex Standard 1 through 3 requirements relating to operating history, bid price, round lot holders, and shares held by the public.\footnote{See Nasdaq Letter supra note 15.}

However, under the NCM standards, an issuer may qualify for listing by satisfying either a shareholder equity requirement (at least $5 million),\footnote{See Amex Rule 101(c)(1).} a market value of listed securities test (at least $50 million),\footnote{See Amex Rule 101(c)(1).} or an income test (at least $750,000 in after tax net income for purposes of Section 18(b) of the Exchange Act).\footnote{24 Nasdaq Rule 4310(c)(3)(A)(iii).}

The Commission notes that the NCM listing standards require at least $50 million in market value of listed securities of $50 million; or (iii) shareholder’s equity of $4 million and a market value of listed securities of $50 million; or (ii) shareholder’s equity of $4 million and a two-year operating history.\footnote{25 See Amex Rule 101(b)(1)(A).} Moreover, Nasdaq’s proposal would increase the aggregate market value of publicly held shares from $5 million to $15 million.\footnote{26 Amex Standard 2 does not require an income test or a market value test but does require an operating history of two years as compared to the NCM, which requires only one year.\footnote{See Nasdaq Proposed Rule Change, supra note 18.} An additional difference is that Amex Standards 2 and 3 require the aggregate market value of publicly held shares to be $15 million, whereas Nasdaq’s requirement is $5 million.\footnote{27 See Amex Rule 101(c)(1).} The Commission preliminarily believes that these differences preclude the Commission from making a determination that the NCM common stock initial listing standards are substantially similar to those of the Amex.

Nasdaq has filed a proposed rule change under Section 19 of the Exchange Act to modify its NCM initial listing standards for common stock. Specifically, Nasdaq’s proposal would require an issuer to have: (i) Shareholder’s equity of $4 million and net income from continuing operations of $750,000 in the most recently completed fiscal year or in two of the last three most recently completed fiscal years; (ii) shareholder’s equity of $4 million and a market value of listed securities of $50 million; or (iii) shareholder’s equity of $5 million and a two-year operating history. Moreover, Nasdaq’s proposal would increase the aggregate market value of publicly held shares from $5 million to $15 million.\footnote{28 See Nasdaq Rule 4310(c)(2)(A)(iii).}
million in scenario (ii) and (iii) above. If these rule changes were approved prior to Commission action on this rule proposal, the Commission preliminarily believes it could find the NCM listing standards for common stock to be substantially similar to those of Amex.

The Commission preliminarily believes that the continued listing requirements for common stock listed on the NCM, while not identical, are substantially similar to those of Amex. Amex’s delisting criteria are triggered by poor financial conditions or operating results of the issuer. Specifically, Amex will consider delisting an equity issue if: (i) Stockholders’ equity is less than $2 million and such issuer has sustained losses from continuing operations and/or net losses in two of its three most recent fiscal years; (ii) stockholders’ equity is less than $4 million and such issuer has sustained losses from continuing operations and/or net losses in three of its four most recent fiscal years; (iii) stockholders’ equity is less than $6 million if such issuer has sustained losses from continuing operations and/or net losses in its five most recent fiscal years; or (iv) the issuer has sustained losses which are so substantial in relation to its overall operations or its existing financial resources, or its financial condition has become so impaired that it appears questionable, in the opinion of the Exchange, as to whether such company will be able to continue operations and/or meet its obligations as they mature.

Although the NCM does not have the same continued listing provisions, Nasdaq also looks at the financial condition and operating results of the issuer. Specifically, for continued inclusion, Nasdaq requires shareholder’s equity of at least $2.5 million, market value of listed securities of at least $35 million, or net income of $500,000 from continuing operations in the past fiscal year or two out of three past fiscal years. Further, Nasdaq requires a minimum bid price for continued listing of $1 per share. In addition, for continued listing, Nasdaq requires an issuer to have a minimum number of publicly held shares of at least 500,000 shares with a market value of at least $1 million.

The Commission preliminarily believes that the differences in the maintenance criteria for common stock listed on Amex and on the NCM are not material and that, taken as a whole, the criteria are substantially similar.

The Commission requests comment on whether the NCM’s common stock listing rules are “substantially similar” to Amex’s rules.

B. Secondary Classes of Common Stock and Preferred Stocks

The Commission notes that only Nasdaq has listing standards for the trading of a secondary class of common stock. A secondary class of common stock is a class of common stock of an issuer that has another class of common stock listed on an exchange. The Commission supported the secondary classes of common stock listing standards of the NCM with the listing standards of the Nasdaq/NGM. The Commission also compared the NCM listing standards for preferred stocks with those of Nasdaq’s NCM.

With respect to the number of round lot holders, bid price, and number of publicly held shares requirements, the Commission preliminarily believes that Nasdaq’s initial and continued listing requirements for secondary classes of common stock and preferred stocks listing on the NCM are substantially similar to the listing standards for the Nasdaq/NGM. The Commission preliminarily believes, however, that the initial and continued listing requirements for market value of publicly held shares for Nasdaq/NGM standards. In particular, the NCM listing standards require that there be at least 200,000 publicly held shares having a market value of at least $2 million for initial listing and 100,000 publicly held shares having a market value of $500,000 for continued listing. The Nasdaq/NGM standards require that there shall be at least 200,000 publicly held shares having a market value of at least $4 million for initial listing and 100,000 publicly held shares having a market value of $1 million for continued listing.

Nasdaq has filed a proposed rule change to increase the requirements for its NCM listing standards for both preferred and secondary classes of common stock for the market value of publicly held shares to $3.5 million for initial listing and $1 million for continued listing. Nasdaq also has proposed to amend its initial and continued NCM listing rules for secondary classes of common stock and preferred stock to require that the common stock or common stock equivalent of the issuer either be listed on Nasdaq or be a covered security as defined in Rule 146(b). Given these proposed revisions to the NCM’s initial and continued listing standards for secondary classes of common stock and preferred stocks, the Commission preliminarily believes it could find that
such standards are substantially similar to those of Nasdaq’s NGM.

The Commission requests comment on whether the NCM secondary classes of common stock and preferred stock rules are “substantially similar” to Nasdaq/NGM’s rules.

C. Convertible Debt

The Commission has compared the NCM listing standards for convertible debt to Amex’s listing standards for debt.\(^47\) The Commission preliminarily does not believe that Nasdaq’s standards are substantially similar to Amex’s standards. Although the NCM’s initial listing standards require a higher level of principal amount outstanding (the NCM standards require $10 million versus $5 million for Amex), Amex also requires that either (i) the issuer of the debt security (or an issuer that controls or is under common control with such issuer or that has guaranteed such issuer’s debt) have equity securities listed on the NYSE, Nasdaq/NGM, or, if no NRSRO has guaranteed the debt security, (ii) an issuer of equity securities listed on Amex, the NYSE, or Nasdaq/NGM, or (iii) that the debt security have a certain level of rating.\(^48\)

Specifically, Amex will not list a debt security unless one of the following conditions is met: (i) The issuer of the debt security also has equity securities listed on Amex, the NYSE, or Nasdaq/NGM; (ii) an issuer of equity securities listed on Amex, the NYSE, or Nasdaq/NGM directly or indirectly owns a majority interest in, or is under common control with, the issuer of the debt security; (iii) an issuer of equity securities listed on Amex, the NYSE, or Nasdaq/NGM has guaranteed the debt security; (iv) a nationally recognized securities rating organization (an “NRSRO”) has assigned a current rating to the debt security that is no lower than an S&P Corporation “B” rating, or an equivalent rating by another NRSRO; or (v) if no NRSRO has assigned a rating to the issue, an NRSRO has currently assigned an investment grade rating to an immediately senior issue or a rating that is no lower than an S&P Corporation “B” rating, or an equivalent rating by another NRSRO; or a pari passu or junior issue.\(^49\) This requirement is designed to ensure that the issuer (or guarantor) of a debt security listed on Amex is in reasonably sound financial condition, while also providing Amex with considerable flexibility in determining which debt issues qualify for listing on the Exchange.\(^50\) The Commission preliminarily believes that the absence of these provisions will make the NCM’s initial listing standards for debt securities not substantially similar to those of Amex.

Nasdaq has filed a proposed rule change to adopt a debt rating provision similar to Amex’s provision to make its NCM initial listing standards more comparable to Amex’s initial listing standards.\(^51\) In light of this proposal, the Commission preliminarily believes it could find that the NCM’s listing standards for convertible debt are substantially similar to those of Amex.

The Commission preliminarily believes that the continued listing requirements for convertible debt securities listed on the NCM are substantially similar to the Amex requirements. The NCM requires that the principal amount outstanding be maintained at $5 million.\(^52\) Amex generally will delist a bond if the aggregate market value or the principal amount of the bond publicly held is less than $400,000, or if the issuer is not able to meet its obligations on the listed debt.\(^53\) Although not identical, the Commission preliminarily believes that both standards are designed to ensure the continued liquidity of the debt security, and are substantially similar.

The Commission requests comment on whether the NCM convertible debt listing rules are “substantially similar” to Amex’s listing standards for debt securities.

D. Warrants

The Commission has compared the NCM’s standards for warrants to Nasdaq’s NGM standards, and preliminarily believes that the NCM’s standards are not substantially similar to the Nasdaq/NGM standards. The NCM initial listing standards require that 100,000 warrants be outstanding for initial listing, whereas Nasdaq/NGM requires that there be 450,000 warrants outstanding.\(^54\) Further, the NCM standards require the issuer’s underlying security to be traded on Nasdaq/NGM, NCM, GSM or any national securities exchange.\(^55\) Nasdaq therefore allows the underlying security to be traded on markets that the Commission has not determined to be substantially similar to Amex, the NYSE, or Nasdaq/NGM under Rule 146(b).\(^56\) In addition, the NCM does not have any continuing maintenance standards for warrants whereas Nasdaq/NGM requires that the underlying security of the issuer must continue to be listed on Nasdaq/NGM.\(^57\)

Nasdaq has filed a proposed rule change with the Commission to increase the required number of warrants outstanding for initial listing on the NCM from 100,000 to 400,000.\(^58\) Nasdaq’s proposal also would require that the security underlying the warrant that is to be listed on the NCM be a covered security as defined in Rule 146(b) (if it is listed on a market other than Nasdaq).\(^59\) Further, Nasdaq would require that the security underlying the warrant continue to be listed on Nasdaq or be a covered security as defined in Rule 146(b).\(^60\) Given these proposed revisions to the NCM’s warrant listing standards, the Commission preliminarily believes it could find the NCM’s listing standards for warrants to be substantially similar to those of Nasdaq/NGM.

The Commission requests comment on whether the NCM’s listing rules for warrants are “substantially similar” to Nasdaq/NGM’s listing rules.

E. Index Warrants

For index warrants traded on the NCM, Nasdaq has adopted the same standards (both initial and continuing) that it applies to index warrants traded...
on the Nasdaq/NGM market. Therefore, the Commission preliminarily believes that the listing standards for index warrants traded on the NCM are substantially similar to the standards applicable to index warrants traded on the Nasdaq/NGM market.

F. Units

The NCM, Amex, and Nasdaq/NGM all evaluate the initial and continued listing of a unit by looking to its components. If all of the components of a unit individually meet the standards for listing, then the unit would meet the standards for listing. The Commission preliminarily believes that it would be able to make a finding that the NCM listing standards for units are substantially similar to a Named Market in light of Nasdaq’s proposed revisions to its NCM’s listing standards for the different categories of securities that could make up the components of a unit, as discussed above.

G. Other Changes

Sections (b)(1) and (b)(2) of Rule 146 use the term “Nasdaq/NMS” to refer to the National Market System of The NASDAQ Stock Market LLC. In addition, Rule 146(b)(1)(i) refers to the Pacific Exchange Incorporated, Rule 146(b)(1)(ii) refers to the Philadelphia Stock Exchange, Incorporated, and Rule 146(b)(1)(iv) refers to the International Securities Exchange, Incorporated. As noted above, on July 1, 2006, what was the National Market System of The NASDAQ Stock Market LLC became known as the Nasdaq Global Market. Further, in April 2006, the Pacific Exchange, Incorporated was renamed NYSE Arca, Inc., and in September 2006, the International Securities Exchange, Incorporated was renamed the International Securities Exchange, LLC. The proposed rule change includes changes to Rule 146(b) to account for these name changes. Finally, the proposal includes a change to reflect the legal name of the Philadelphia Stock Exchange, Inc.

H. Comments

The Commission has received three comment letters on Nasdaq’s petition. The State Regulation of Securities Committee of the American Bar Association Section of Business Law (“ABA Committee”) expressed support of the petition, assuming that Nasdaq’s representation of the data and analysis contained in the petition is accurate. The North American Securities Administrator’s Association (“NASAAA”), stated that it does not oppose the Nasdaq petition but is concerned generally about what it perceives to be deficiencies in listing standards at several of the Named Markets and encourages the Commission to undertake an SRO oversight initiative to set uniform principles for these Named Markets.

IV. Solicitation of Comments

The Commission seeks comment generally on the desirability of amending Rule 146(b) to include securities of the NCM. As discussed above, based on its review of Nasdaq’s listing rules for its NCM, the Commission preliminarily believes that the current original and continued listing standards for the NCM are not substantially similar to those of the Amex, the NYSE, or Nasdaq/NGM. The Commission seeks comments on its preliminary analysis. The Commission also seeks comments on whether the proposed changes to its NCM standards that Nasdaq has filed would make the NCM’s initial listing and continued listing standards substantially similar to those of a Named Market. In addition, if the NCM securities are designated as covered securities under Rule 146(b)(1), then the NCM’s listing standards would be subject to Rule 146(b)(2) under the Securities Act. Rule 146(b)(2) conditions the designation of securities as “covered securities” under Rule 146(b)(1) on the identified exchange’s listing standards continuing to be substantially similar to those of the Named Markets. Thus, under Rule 146(b)(2), the designation of certain securities as covered securities would be conditioned on Nasdaq maintaining listing standards for NCM securities that were found to be substantially similar to those of the Named Markets. Commenters may wish to address the application and effect of Rule 146(b)(2) on the proposal.

The Commission also invites commenters to provide views and data as to the costs, benefits, and effects associated with the proposed amendments. In addition to the questions posed above, commenters are welcome to offer their views on any other matter raised by the proposed amendment to Rule 146(b). Finally, the Commission requests comment on whether it could use a different methodology to determine whether the NCM’s listing standards are “substantially similar” to the Named Markets.

V. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 does not apply because the proposed amendment to Rule 146(b) does not impose recordkeeping or information collection requirements or other collection of information, which require the approval of the Office of Management and Budget under 44 U.S.C. 3501 et seq.

VI. Cost and Benefits of Proposed Rulemaking

Congress amended Section 18 of the Securities Act to exempt covered securities from state registration requirements. These securities are listed on the Named Markets or any other national securities exchange determined by the Commission to have substantially similar listing standards to the Named Markets. Consistent with statutory authority, the Commission proposes to determine (if the Commission were to approve the rule changes that Nasdaq has filed) that the listing standards for securities listed on the NCM are substantially similar to those of either Amex, the NYSE, or Nasdaq/NGM. Securities listed on the NCM therefore would be covered securities subject only to federal regulation.

By exempting securities listed on the NCM from state law registration requirements, the Commission expects that the listing process for those securities would become easier as one layer of regulation is eliminated. Moreover, the Commission also expects...
adoption of the rule would reduce the administrative burden the issuers of covered securities face inasmuch as compliance with state blue sky law requirements would be preempted.71

The Commission also preliminarily believes that the proposed amendment to Rule 146(b) should permit Nasdaq to compete with other markets whose listed securities are exempt from state law registration requirements for new securities products and listings. This result would likely enhance competition and, potentially, liquidity, thus benefiting market participants and the public. The proposed amendment would eliminate state registration of securities listed on the NCM. There may be a cost to investors through the loss of benefits of state registration and oversight, although the cost is difficult to quantify. The Commission believes that Congress contemplated these costs in relation to the economic benefits of exempting covered securities from state regulation. The Commission, however, is considering the costs and benefits of the proposed amendment to Rule 146(b) and requests commenters to provide views and supporting information as to the costs and benefits associated with this proposal.

VII. Consideration of Promotion of Efficiency, Competition, and Capital Formation

As required under the Securities Act,72 the Commission has preliminarily considered the proposed rule’s impact on efficiency, competition, and capital formation. National securities exchanges compete for the listing of securities. Thus, the Commission preliminarily believes that amending Rule 146(b) to designate securities traded on the NCM as covered securities (if the Commission were to approve the rule changes that Nasdaq has filed) would offer potential benefits for investors because it would facilitate the ability of Nasdaq to compete for listings, which should increase competition and enhance the overall liquidity, and thus the efficiency of the U.S. securities markets. The Commission also preliminarily believes that the proposed rule would serve to reduce the cost of raising capital because it would streamline the registration process for issuers listing on the NCM. In addition, the Commission believes that the proposed rule amendment, consistent with Congressional action, is designed to promote efficiency by reducing a layer of duplicative regulation. The Commission also preliminarily believes that the proposed amendment to Rule 146(b) should permit Nasdaq to compete with other markets whose securities are exempt from state law registration requirements for new securities products and listings. Finally, the proposed amendment to Rule 146(b) should not impair efficiency, competition, and capital formation because it would impose no recordkeeping or compliance burdens, but would provide a limited purpose exemption under the federal securities laws.

Thus, the Commission preliminarily believes that the proposed amendment to Rule 146(b) would promote efficiency, competition, and capital formation. Commenters should consider the proposed amendment’s effect on efficiency, competition, and capital formation.

VIII. Regulatory Flexibility Act Certification

Section 603(a) of the Regulatory Flexibility Act73 requires the Commission to undertake an initial regulatory flexibility analysis of the proposed amendment to Rule 146 on small entities, unless the Commission certifies that the proposed amendment, if adopted, would not have a significant economic impact on a substantial number of small entities.74 For purposes of Commission rulemaking in connection with the Regulatory Flexibility Act, an issuer is a small business if its “total assets on the last day of its most recent fiscal year were $5 million or less.”75 An exchange is a small business if it has been exempt from the reporting requirements of Rule 60176 and it is not affiliated with any person other than a natural person that is not a small business.77 The Commission believes that the proposal to amend Rule 146(b) would not affect a substantial number of small entities because to list its securities on the NCM, an issuer’s aggregate market value of publicly held shares must be at least $5 million.78 If an entity’s market value of publicly held shares is at least $5 million, it is reasonable to believe that its assets are worth at least $5 million. Therefore, an entity seeking to list securities on the NCM generally will have assets with a market value of at least equal to $5 million and thus would not be considered a small entity. Further, Nasdaq itself is not a small entity for purposes of the RFA.79

Accordingly, the Commission hereby certifies, pursuant to Section 605(b) of the Regulatory Flexibility Act,80 that amending Rule 146(b) as proposed would not have a significant economic impact on a substantial number of small entities. The Commission encourages written comments regarding this certification. The Commission solicits comment as to whether the proposed amendment to Rule 146(b) could have an effect that has not been considered. The Commission requests that commenters describe the nature of any impact on small entities and provide empirical data to support the extent of such impact.

IX. Small Business Regulatory Enforcement Fairness Act of 1996

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, a rule is “major” if it results or is likely to result in:

(i) An annual effect on the economy of $100 million or more;
(ii) A major increase in costs or prices for consumers or individual industries; or
(iii) Significant adverse effects on competition, investment, or innovation.81

The Commission requests comment regarding the potential impact of the proposed amendment on the economy on an annual basis. Commenters should provide empirical data to support their views to the extent possible.

X. Statutory Authority

The Commission is proposing an amendment to Rule 146 pursuant to the Securities Act of 1933,82 particularly Sections 18(b)(1)(B) and 19(a).83

Text of the Proposed Rule

List of Subjects in 17 CFR Part 230

Securities.

For the reasons set forth in the preamble, Title 17, Chapter II of the Code of Federal Regulations is proposed to be amended as follows:

72 A 1996 Report relating to Securities Market Reform: State Registration of Securities—Costs and Benefits stated that up to 1 percent of an issue’s cost, which is generally covered by the offering’s underwriter, could be apportioned to the legal/administrative costs of state level regulation. One benefit of this proposal would be to eliminate this type of legal/administrative cost with respect to NCM securities.
74 5 U.S.C. 605(b).
75 17 CFR 230.157. See also 17 CFR 240.0–10(a).
76 17 CFR 242.601 (formerly Rule 11Aa3–1 under the Act).
77 17 CFR 240.0–10(e).
78 As of June 30, 2006, the Division estimates that there were 557 listed issuers of securities on the NCM.
79 5 U.S.C. 603(a).
80 5 U.S.C. 605(b).
82 15 U.S.C. 77a et seq.
83 15 U.S.C. 77b(b)(1)(B) and 77a(a).
PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

1. The general authority citation for Part 230 is revised to read as follows:

Authority: 15 U.S.C. 77b, 77c, 77d, 77f, 77g, 77h, 77j, 77r, 77s, 77z–3, 77sss, 78c, 78d, 78j, 78l, 78m, 78n, 78o, 78l, 78w, 78ll(d), 78mm, 80a–8, 80a–24, 80a–28, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

2. Section 230.146 is amended by revising paragraphs (b)(1) and (b)(2) to read as follows:

§ 230.146 Rules under Section 18 of the Act.

(b) * * *

(1) For purposes of Section 18(b) of the Act (15 U.S.C. 77r), the Commission finds that the following national securities exchanges, or segments or tiers thereof, have listing standards that are substantially similar to those of the New York Stock Exchange (“NYSE”), the American Stock Exchange (“Amex”), or the National Market System of the Nasdaq Stock Market (“Nasdaq/NGM”), and that securities listed on such exchanges shall be deemed covered securities:

(i) Tier I of the NYSE Arca, Inc.;
(ii) Tier I of the Philadelphia Stock Exchange, Inc.;
(iii) The Chicago Board Options Exchange, Incorporated;
(iv) Options listed on the International Securities Exchange, LLC; and

(2) The designation of securities in paragraphs (b)(1)(i) through (v) of this section as covered securities is conditioned on such exchanges’ listing standards (or segments or tiers thereof) continuing to be substantially similar to those of the NYSE, Amex, or Nasdaq/NGM.

Dated: November 16, 2006.

By the Commission.

Nancy M. Morris,
Secretary.

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