

August 27, 2008

SEC Adopts New Rules Affecting Foreign Private Issuers

At today's Open Meeting, the Securities and Exchange Commission (SEC) unanimously approved amendments to certain rules and forms in an effort to modernize its disclosure requirements for foreign companies. Specifically, the SEC adopted rules

- significantly revising the Rule 12g3-2(b) exemption from Exchange Act registration and reporting requirements;
- changing the timing for the determination of foreign private issuer status, shortening the deadline for filing annual reports on Form 20-F, eliminating certain Form 20-F provisions that accorded limited accounting relief to certain foreign private issuers, and creating several new Form 20-F disclosure requirements; and
- revising the current exemptions for cross-border business combination transactions and rights offerings to expand and enhance the usefulness of the exemptions, and to adopt changes to the beneficial ownership reporting rules to permit certain foreign institutions to file reports on a shorter form.

The SEC received numerous comments on the proposed rules. The vast majority of these comments praised the SEC's recent efforts to improve the accessibility of the U.S. capital markets to foreign private issuers and to update its rules to reflect advances in technology and to respond to the increasing globalization of the capital markets. However, each of the proposals received criticisms, and the SEC did modify certain of the proposals, in some respects, from the versions originally issued for public comment.

The text of the final rules is not yet available, so the descriptions provided in this special alert are based on the SEC's press release announcing the rule amendments¹ and statements made by the SEC commissioners and staff at the Open Meeting.

Amendments to Rule 12g3-2(b)

In February, the SEC proposed to amend Rule 12g3-2(b), which currently permits a foreign private issuer to exceed the shareholder thresholds for registration under Section 12(g) of the Exchange Act, effectively permitting its equity securities to be traded on a limited basis in the over-the-counter market in the United States. The proposed amendments were adopted substantially as proposed, except that

¹ See SEC News Release 2008-183, available at <http://www.sec.gov/news/press/2008/2008-183.htm> (Aug. 27, 2008).

the SEC, in response to significant opposition from commenters, did abandon a proposed condition that would have depended on the issuer's average daily U.S. trading volume. That condition would have required that the average daily U.S. trading volume for the subject class of securities be no greater than 20 percent of the average daily trading volume of that class of securities worldwide for the issuer's most recently completed fiscal year.

The final rules will eliminate existing Rule 12g3-2 paper submission requirements by automatically granting the Rule 12g3-2(b) exemption to a foreign private issuer that meets specified conditions, which would not depend on the number of an issuer's U.S. security holders, but which would require an issuer to publish electronically, and in English, specified non-U.S. disclosure documents.

In order to be eligible to claim the Rule 12g3-2(b) exemption, an issuer must

- not be subject to any other reporting obligations under Section 13(a) or 15(d) of the Exchange Act, as is the case under the existing rule;²
- maintain a listing of the subject securities on one or more exchanges in one or two foreign jurisdictions comprising its primary trading market;³ and
- publish specified non-U.S. disclosure documents in English on its Internet Web site or through an electronic information delivery system that is generally available to the public in its primary trading market, unless the issuer is claiming the exemption in connection with, or recently following, its deregistration.

In order to maintain the Rule 12g3-2(b) exemption, an issuer must

- electronically publish specified non-U.S. disclosure documents in English for subsequent fiscal years on an ongoing basis;
- continue to satisfy the foreign listing condition as described above; and
- not otherwise become subject to any other Exchange Act reporting obligations.

The final rules will establish a three-year transition period to accommodate a currently exempt issuer that could lose the exemption upon the effective date of the revised rule because it did not satisfy a requirement of the revised rule. In addition, to provide time for issuers to make arrangements for required documents to be translated into English and made electronically available, the final rule will establish a three-month transition period following its effectiveness, during which the SEC's staff will continue to process paper submissions

² Accordingly, issuers with any class of debt or equity securities that are listed on a national securities exchange or who have otherwise registered a class of securities under the Exchange Act (e.g., in order to facilitate trading on the OTC Bulletin Board) will continue to be ineligible to claim the Rule 12g3-2(b) exemption.

³ As is the case under the SEC's existing foreign issuer deregistration rules, "primary trading market" in this instance means that an aggregate of at least 55 percent of the trading in the subject class of securities took place in the referenced one or two jurisdictions during a recent 12-month period, as long as at least one of those jurisdictions carries more trading for the issuer than the United States trading markets.

under Rule 12g3-2(b). Following that three-month period, the SEC will no longer process paper submissions under Rule 12g3-2(b).

Foreign private issuers that currently rely on the Rule 12g3-2(b) exemption should immediately assess their ability to comply with the English language disclosure and electronic posting requirements. Those issuers that do not currently maintain a foreign listing (or whose foreign listing(s) will not qualify under the primary trading market test) should begin consideration of possible alternatives, which may include seeking a qualifying listing within the three-year transition period or taking necessary action (which may include terminating a sponsored American Depositary Receipts program) to ensure that they will qualify for another available exemption, such as Rule 12g3-2(a), which exempts an issuer with fewer than 300 U.S. holders.

Foreign Issuer Reporting Enhancements

In February, the SEC also proposed various changes to existing rules and forms regarding the timing of determinations of foreign private issuer status, the deadline for filing annual reports on Form 20-F and certain Form 20-F disclosure requirements. The proposed amendments were adopted substantially as proposed, except that the SEC, in response to strong opposition from commenters, did not adopt the proposed requirement that financial statements of significant acquired companies be included in annual reports on Form 20-F, modified the deadline for filing annual reports on Form 20-F and extended the proposed two-year transition period to three years.

The final rules

- permit reporting foreign issuers to assess their foreign private issuer status only once a year, on the last business day of their second fiscal quarter, rather than on a continuous basis, as currently required;
- accelerate the reporting deadline for annual reports filed on Form 20-F from six months to four months after the issuer's fiscal year-end, subject to a three-year transition period;
- amend Form 20-F by eliminating an instruction to Item 17 that permits certain foreign private issuers to omit segment data from their U.S. GAAP financial statements (subject to a three-year transition period) and eliminate the availability of the limited U.S. GAAP reconciliation option that is contained in Item 17 of Form 20-F for foreign private issuers (but that option will remain available for third party financial statements required to be included in Form 20-F);
- amend Exchange Act Rule 13e-3, which pertains to going private transactions by reporting issuers or their affiliates, to reference the deregistration and termination of reporting rules applicable to foreign private issuers that the SEC adopted in late 2007;⁴ and
- amend Form 20-F to require disclosure in annual reports filed on Form 20-F relating to changes in and disagreements with the issuer's certifying accountant, the fees, payments and other charges relating to American Depositary Receipts, and significant differences in corporate governance requirements.

⁴ See Alston & Bird LLP Securities Law Advisory, "SEC Amends Deregistration Rules to Allow Foreign Private Issuers an Easier Exit," available at <http://www.alston.com/files/Publication/72410458-fadf-44c2-991d-01e08c69b53c/Presentation/PublicationAttachment/c7fc0e7a-2aec-4f34-b63a-c9d4334fbc26/New%20FPI%20DeRegistration%20Rules.pdf> (Apr. 3, 2007).

The proposal to accelerate the filing date of annual reports on Form 20-F received the most consistent and vocal opposition. Most commenters noted that the amendment would dramatically reduce the amount of time that foreign private issuers would have to prepare their Form 20-F, in many cases imposing a filing date that is before the required filing date for their home country annual report. Many commenters advocated a Form 20-F filing date that was some defined period of time after the filing of the issuer's home country annual report to provide the issuer with sufficient time for preparation for GAAP reconciliations and English translations. However, the SEC expressly rejected that alternative in favor of a uniform four-month filing deadline. To provide additional incentive for issuers to adopt International Financial Reporting Standards (IFRS), as adopted by the Independent Accounting Standards Board, the SEC extended the proposed two-year transition period to three years, which generally coincides with the 2011 IFRS implementation deadline in many foreign jurisdictions.

Additionally, the SEC tabled the proposed amendment requiring issuers to present information about completed acquisitions that are significant at the 50 percent or greater level, in response to commenter concerns about the ability of issuers to perform the required audits on a timely basis, and questions regarding the relevance of those financial statements to investors.

Current Form 20-F filers should begin analyzing how they will adjust their disclosure processes to accommodate the new Form 20-F filing deadline. In addition, issuers should prepare for the new disclosure requirements relating to accountant changes, ADR fees and corporate governance differences. Issuers should take particular note of the disclosures regarding changes in and disagreements with their certifying accountants, which are modeled on existing Form 8-K disclosure requirements and require more extensive disclosures about the outgoing auditors than is required in most other countries.

Finally, those issuers that relied upon the segment reporting and U.S. GAAP reconciliation relief provided in Item 17 of Form 20-F should begin assessing how they will comply with the requirements to provide full U.S. GAAP reconciliations and segment information under Item 18. Potentially most significant will be the U.S. GAAP footnote requirements, which may be challenging for issuers that file on the basis of local GAAP and utilize Item 17.

Amendments to Cross-Border Tender Offer Rules

In May, the SEC proposed various changes to (1) the current exemptions for cross-border business combination transactions and rights offerings to generally provide for an expansion of the exemptions for Tier I and Tier II cross-border transactions, including the codification of certain interpretive positions and exemptions frequently granted by the SEC in cross-border transactions, and (2) the beneficial ownership reporting rules to permit certain foreign institutions to file reports on a Schedule 13G. Additionally, the SEC proposed to issue interpretive guidance on various topics relating to cross-border transactions.⁵

⁵ See Alston & Bird LLP Securities Law Advisory, "SEC Proposes Changes to Cross-Border Tender Offer Rules," available at <http://www.alston.com/files/Publication/c284dc8b-6be6-4bbd-bcd2-4192c01ed1f6/Presentation/PublicationAttachment/d36b3fa3-936f-4cd5-ab36-436fa2916da2/Cross%20Border%20Advisory.pdf> (June 3, 2008).

The proposed amendments and interpretive guidance were adopted substantially as proposed, such that they retain the two-Tier structure based on applicable U.S. ownership thresholds, but modify the procedures used to calculate U.S. ownership as well as expand the availability and scope of the exemptions.

The final rules

- refine the tests for calculating U.S. ownership of the target company for purposes of determining eligibility to rely on the cross-border exemptions in both negotiated and hostile transactions, including changes to
 - allow the use of the date of public announcement of the business combination as the reference point for calculating U.S. ownership;
 - permit the offeror to calculate U.S. ownership as of a date within a 60-day range before announcement; and
 - specify when the offeror has reason to know certain information about U.S. ownership that may affect its ability to rely on the presumption of eligibility in non-negotiated tender offers;
- expand relief under Tier I for affiliated transactions subject to Rule 13e-3 of the Exchange Act for transaction structures not covered under current cross-border exemptions, such as schemes of arrangement, cash mergers or compulsory acquisitions for cash;
- extend the specific relief afforded under Tier II to tender offers not subject to Sections 13(e) or 14(d) of the Exchange Act;
- expand the relief afforded under Tier II in several ways to eliminate recurring conflicts between U.S. and foreign law and practice, including
 - allowing more than one offer to be made abroad in conjunction with a U.S. offer;
 - permitting bidders to include foreign security holders in the U.S. offer and U.S. holders in the foreign offer(s);
 - allowing bidders to suspend back-end withdrawal rights while tendered securities are counted;
 - allowing subsequent offering periods to extend beyond 20 U.S. business days;
 - allowing securities tendered during the subsequent offering period to be purchased within 14 business days from the date of tender;
 - allowing bidders to pay interest on securities tendered during a subsequent offering period;
 - allowing separate offset and proration pools for securities tendered during the initial and subsequent offering periods;

- codify existing exemptive orders with respect to the application of Rule 14e-5 of the Exchange Act for Tier II tender offers;
- expand the availability of early commencement to offers not subject to Section 13(e) or 14(d) of the Exchange Act;
- require that all Form CBs and the Form F-Xs that accompany them be filed electronically;
- modify the cover pages of certain tender offer schedules and registration statements to list any cross-border exemptions relied upon in conducting the relevant transactions; and
- permit foreign institutions to report on Schedule 13G to the same extent as their U.S. counterparts, without individual no-action relief.

At the Open Meeting, the SEC also adopted interpretive guidance related to cross-border transactions, including the application of the “all-holders” rules to foreign target security holders, the ability of bidders to exclude U.S. target security holders in cross-border tender offers and exchange offers and the use of vendor placement procedures by bidders in exchange offers to avoid the registration requirements of the Securities Act.

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