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Bulletins

SEC Liberalizes Rules for Deregistration of Foreign Private Issuers

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SEC Liberalizes Rules for Deregistration of Foreign Private Issuers

On March 21, 2007, the Securities and Exchange Commission (the "SEC") adopted amendments to the rules governing when a foreign private issuer[1] may deregister its securities under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These new rules significantly ease the deregistration process compared to both current rules and revised rules that the SEC proposed in December 2005. They are quite similar to re-proposed rules that the SEC published in December 2006, with some helpful technical amendments and transitional relief.

Most notably, the new rules allow eligible foreign private issuers to use a new benchmark for deregistration based on U.S. average daily trading volume ("ADTV") relative to worldwide ADTV rather than on the number of U.S. securityholders. Under the new rules, a foreign private issuer may deregister if, during the 12-month period ending 60 days before filing for deregistration, its U.S. ADTV was 5% or less of its worldwide ADTV, regardless of the total number of U.S. residents holding its securities. The new rules also enable foreign private issuers to terminate, rather than merely suspend, their Exchange Act reporting obligations.

The adopting release for the new rules is expected by mid-April, and the new rules will be effective 60 days after publication of the adopting release. This timing would enable eligible calendar year filers to avoid filing a 2006 Form 20-F at the end of June.

Background

Generally, a foreign private issuer becomes subject to SEC registration and reporting under the Exchange Act if the issuer (i) has securities listed on a U.S. national securities exchange, (ii) offers securities publicly in the U.S. or (iii) has more than a specified number of securityholders in the U.S.

Under current Exchange Act rules, terminating Exchange Act registration and associated reporting obligations can be a long and complicated process for a foreign private issuer. A foreign private issuer may exit the Exchange Act reporting regime only when its securities are neither listed on any U.S. national securities exchange nor held by more than 300 U.S. residents. To determine whether 300 U.S. residents are securityholders, the foreign private issuer must look through the record ownership of institutional and nominee holders on a worldwide basis. This often proves a difficult and costly proposition. Also, the 300-securityholder threshold may be difficult to avoid in today's global securities markets, even for companies that have little U.S. investor interest relative to their overall securityholder base. Furthermore, a foreign private issuer may only suspend, and not terminate, its Exchange Act reporting obligations.

The New Rules

Deregistration of Equity Securities

The SEC has adopted new Exchange Act Rule 12h-6, which permits foreign private issuers to terminate their reporting obligations regarding a class of equity securities based solely on an ADTV test. Alternatively, foreign private issuers may continue to rely on a 300- securityholder test that is similar to the test currently in effect.

U.S. Average Daily Trading Volume Benchmark

Under the new rules, a foreign private issuer's equity securities are eligible for deregistration if the ADTV of the securities in the U.S. (including off-exchange trading) represents 5% or less of the ADTV of those securities worldwide during the 12 month period ending within 60 days of an application for deregistration. This new benchmark allows a foreign private issuer to terminate its Exchange Act obligations regardless of the number of U.S. residents holding that security.

Differences from December 2006 Proposal

This standard is a further liberalization from the standard proposed in December 2006, in three key ways:

- the 5% benchmark is measured against worldwide ADTV, rather than primary trading market[2] ADTV as proposed in December 2006;
- off-exchange trading counts in worldwide ADTV calculations, so long as the source of trading information is reliable and not duplicative of exchange-reported trading; and
- trading in convertible and other equity-linked securities need not be counted.

A Possible Waiting Period—But with Transitional Relief

In order to take advantage of the new ADTV test, a foreign private issuer must wait 12 months from the date that it has either (i) delisted its securities from a U.S. exchange or (ii) terminated a sponsored American Depositary Receipt ("ADR") facility if, during the 12 months preceding the delisting or facility termination, its U.S. ADTV exceeded 5% of its worldwide ADTV. The rules proposed in December 2006 would also have imposed a waiting period in respect of an ADR termination even if the issuer did not exceed the 5% threshold when the termination occurred. In another helpful departure from the December 2006 proposal, the waiting period will not apply to issuers that delisted or terminated their ADR programs within the 12 months preceding the adoption of the rules.

Alternative 300 Holder Benchmark

As an alternative to the ADTV benchmark and as long as the issuer meets certain other conditions under Rule 12h-6, a foreign private issuer may terminate its Exchange Act reporting obligations regarding a class of equity securities if it has fewer than 300 record holders on a worldwide basis or who are U.S. residents.

This alternative benchmark is similar to the current standard for deregistration. Significantly, however, the new rules modify the method for determining the number of U.S. resident securityholders by allowing issuers to limit their "look-through" inquiries to brokers, banks and other nominees located in the U.S., the issuer's jurisdiction of organization and the jurisdiction of its primary trading market. If after reasonable diligence, the issuer is unable without unreasonable effort to obtain information about the identity and residence of the underlying securityholders, the issuer may assume that the securityholders reside in the jurisdiction where the nominees have their principal place of business. Issuers may also rely in good faith on data from third-party providers that specialize in collecting securityholder information.

Other Conditions

A foreign private issuer intending to deregister and terminate its Exchange Act reporting obligations for equity securities must also meet the following conditions:

- the issuer must have been a reporting company for at least one year, have filed or submitted all required reports during that year and have filed at least one annual report;
- the securities of the issuer must not have been sold in an offering in the U.S. that is registered under the Securities Act of 1933, as amended, during the preceding 12 months, except for certain types of offerings including offerings pursuant to option plans, selling securityholder resales, rights offerings and conversions of outstanding securities;
- the issuer must have maintained a listing for a least a year in a non-U.S. jurisdiction that, either alone or together with one other non-U.S. jurisdiction, constitutes the primary trading market for the subject class of securities; and
- the issuer must publicly announce its intention to deregister on or before the date it files to deregister using Form 15F (as described below), which announcement itself must be filed, either under cover of Form 6-K or as an exhibit to the Form 15F.

Deregistration of Debt Securities

The new rules also permit a foreign private issuer to terminate its Exchange Act reporting obligations with respect to a class of debt security where:

- the issuer has filed or furnished all required reports under the Exchange Act, including at least one Exchange Act annual report; and
- the debt securities are held of record by either fewer than 300 holders on a worldwide basis or fewer than 300 persons residing in the U.S. (using a counting method similar to the one for equity holders described above).

New Benefits to Successor Issuers

An issuer that succeeds to Exchange Act requirements as a result of a business combination will be able to use the new rules immediately after succession so long as it meets the foreign listing and quantitative standards of Rule 12h-6 itself, and so long as the acquired company met the one-year reporting requirement. However, if such an issuer effected the business combination through its own U.S.-registered offering, a new one-year reporting period would be triggered, so the issuer would not be able to use the successor provision.

Immediate Use of 12g3-2(b) Exemption

The availability of the exemption from Exchange Act registration and reporting under Rule 12g3-2(b) promulgated under the Exchange Act will be significantly extended under the new rules. This exemption allows foreign private issuers, regardless of the number of their U.S. securityholders, to avoid Exchange Act registration so long as they are not listed on a U.S. exchange and they provide home-market disclosures to the SEC in English (in certain cases in summary form where the source material is not in English). The 12g3-2(b) exemption is currently available only to issuers that have not been registered under Section 12 of the Exchange Act for the past 18 months and that have no reporting obligation, suspended or active, under Section 15(d) of the Exchange Act.

The new rules allow immediate and automatic use of 12g3-2(b) after deregistration, so long as the issuer publishes English disclosures required under 12g3-2(b) on its Internet website or through an electronic information delivery system generally available to the public rather than simply furnishing them to the SEC.

Mechanics for Deregistration

In order to deregister its securities, a foreign private issuer will be required to file a Form 15F with the SEC certifying that at the date of filing it meets the conditions for terminating its Exchange Act registration and reporting obligations. Filing of the Form 15F automatically suspends an issuer's reporting obligations regarding the class of security in question. If the SEC does not object within 90 days of the filing of the Form 15F, the suspension becomes a permanent termination. If the SEC were to reject the Form 15F, the issuer would have 60 days to file or submit all reports that would have been required had the Form 15F not been filed. The issuer is under no duty to monitor its eligibility for deregistration during the 90-day waiting period, but if it obtains actual knowledge of information that causes it reasonably to believe it was not eligible for deregistration at the time of filing its Form 15F it must withdraw the Form 15F before effectiveness.

Effect on Form 15 Applicants under Prior Rules

An issuer that deregistered under the prior rules is eligible to use Form 15F to terminate its Exchange Act obligations permanently, so long as it does not have any current Exchange Act registration or reporting requirements and meets the 12-month foreign listing requirement that applies to first-time deregistrants on Form 15F.

Footnotes

[1]A "foreign private issuer" is an issuer incorporated or organized under the laws of a non-U.S. jurisdiction that either (i) has 50% or less of its outstanding voting securities held of record by U.S. residents or (ii) has more than 50% of its outstanding voting securities held by U.S. residents and has (a) a majority of its executive

officers or directors be non-U.S. citizens or residents; (b) 50% or more of its assets located outside the U.S.; and (c) its business administered principally outside the U.S.

[2]The "primary trading market," as defined by the SEC, is the securities market in which at least 55% of the trading in the relevant securities has taken place during a recent twelve-month period. An issuer may aggregate trading in up to two foreign jurisdictions for the purpose of meeting this trading volume condition, provided that the trading market in at least one of the two foreign jurisdictions must be larger than the U.S. trading market for the issuer's securities.