

July 19, 2007

## SEC Proposes to Eliminate Reconciliation Requirement for IFRS Financial Statements

The SEC has published for public comment a proposal that would allow foreign private issuers to file their financial statements without reconciliation to U.S. generally accepted accounting principles (“U.S. GAAP”), as currently required by Form 20-F. The relief would only be available to foreign private issuers that file their financial statements in full compliance with the English language version of International Financial Reporting Standards (“IFRS”), as published by the International Accounting Standards Board (“IASB”).

### I. Current SEC Requirements on Reconciliation to U.S. GAAP

Under current rules, foreign private issuers that register their securities with the SEC, and that are obligated to file periodical reports under Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (“Exchange Act”), are required to reconcile to U.S. GAAP the financial statements that they file with the SEC if such financial statements are prepared using any basis of accounting other than U.S. GAAP.

The principal requirements for financial statements filed by foreign private issuers are described in Items 17<sup>1</sup> and 18<sup>2</sup> of Form 20-F. Under Item 17(c)(2), financial statements and schedules required to be furnished by Form 20-F may be prepared (a) under U.S. GAAP or (b) under generally accepted accounting principles of another jurisdiction with a reconciliation of specific items to U.S. GAAP. In the latter case, the filer is required to provide a discussion on the reconciling differences including the description and quantification of each material variation and a prominent legend, or an indication in the audit report, of the accounting principles used in the preparation of the financial statements. Under Item 18(b), the filer must provide the information specified in Item 17 as well as other disclosure required by Regulation S-X and U.S. GAAP.

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<sup>1</sup> An issuer may use Item 17 when filing its financial statements in an Exchange Act registration statement or an annual report filed under Form 20-F, or as part of a Securities Act registration Statement for investment grade, non-convertible securities or certain rights offerings.

<sup>2</sup> An issuer must comply with Item 18 when filing financial statements in a Securities Act registration statement for offerings of equity, convertible and other securities.

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## **II. Summary of the Eligibility Requirements for Foreign Private Issuers to Use IFRS without Reconciliation to U.S. GAAP**

Only foreign private issuers filing their financial statements in full compliance with the English language version of IFRS as published by IASB would be permitted to file financial statements without reconciliation to U.S. GAAP (as required under Items 17 or 18 of Form 20-F, as applicable). Note that the amendments would apply to an eligible issuer regardless of whether such issuer complies with IFRS on a voluntarily basis or in compliance with any requirement of its home country or stock exchange where its securities are listed.

Foreign private issuers would be required to state unreservedly and explicitly and in a prominent footnote to their financial statements that such financial statements are in compliance with IFRS as published by IASB. Furthermore, the independent auditor of the company must render an opinion stating that the issuer's financial statements comply with IFRS (as published by IASB).

A foreign private issuer that is eligible to avoid reconciling its IFRS financial statements would be allowed to reconcile its financial statements to U.S. GAAP if it chooses. In such case, the foreign private issuer would have to rely on the current requirements of Items 17 and 18 of Form 20-F.

## **III. Proposed Amendments to Form 20-F and Conforming Changes to Regulation S-X and other SEC Rules and Forms**

The SEC has proposed to revise Item 17(c)(2) of Form 20-F to allow foreign private issuers that file financial statements that comply with the English language version of IFRS as published by the IASB to file their financial statements in annual filings and registration statements without reconciliation to U.S. GAAP. The SEC has also proposed to revise Item 18(b) such that the disclosures otherwise required by U.S. GAAP and Regulation S-X would not be required if a filer provides financial statements using IFRS as published by IASB.

Under the proposal, foreign private issuers that would be eligible to avoid reconciling their annual financial statements to U.S. GAAP would also be able to avoid reconciling their interim period financial statement to U.S. GAAP (as long as such financial statements are prepared in accordance with IFRS as published by IASB). The Form 20-F requirement to provide U.S. GAAP reconciliation or reverse reconciliation when local GAAP statements are more recent than the financial statements in an SEC filing continues to apply.

In addition, the SEC has proposed to revise the instruction to Item 3.A<sup>3</sup> of Form 20-F to clarify that selected financial data based on the U.S. GAAP reconciliation is required only if the filer prepares its primary financial statements using a basis of accounting other than IFRS as published by IASB.

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<sup>3</sup> Item 3.A of Form 20-F requires foreign private issuers to provide five years of selected financial data.

Note that a foreign private issuer that is eligible to avoid reconciling to U.S. GAAP would nonetheless, under the SEC proposal, be required to respond to the items of Form 20-F that refer to U.S. GAAP pronouncements, such as Item 11 (“Qualitative and Quantitative Disclosures about the Market Risk”) and disclosure of off-balance sheet arrangements under Item 5 (“Operating and Financial Review and Prospects”). In providing that disclosure, however, the issuer should apply the IFRS notion of the principles embodied in the relevant U.S. GAAP pronouncements.

The SEC has also proposed amending Item 18 of Form 20-F to clarify that any filer that provides disclosure under FAS 69 (“Disclosures about Oil and Gas Producing Activities”) is still required to disclose the information called for under such statement even though the filer is preparing financial statements in accordance with IFRS as published by the IASB.

For first time IFRS adopters, the proposals do not affect the applicability of General Instruction G to Form 20-F, which permits foreign private issuers, for their first year of reporting under IFRS as adopted by IASB, to file two years rather than three years of statements of income, changes in shareholders’ equity and cash flows prepared in accordance with IFRS. Therefore, the SEC has proposed conforming amendments to clarify that the U.S. GAAP reconciliation requirement is not applicable to eligible issuers that may also be eligible to rely on General Instruction G.

It should be noted that Regulation S-X, other than its form and content requirements, will continue to apply under the proposed amendments. For example, the requirements relating to financial statements of acquired/disposed entities (under Rule 3-05 of Regulation S-X) and financial statements for issuers of guaranteed securities and guarantors (under Rule 3-10 of Regulation S-X) will continue to apply. In applying these rules, however, issuers will be able to utilize financial information prepared under IFRS. Specifically in the case of pro forma financial information, pro forma results must be presented using the same basis of accounting as the issuer since the requirements for pro forma financial information under Article 11 of Regulation S-X continue to be governed by the financial statements of the issuer. Accordingly, a foreign private issuer using IFRS as published by the IASB as its basis of accounting would need not to reconcile its pro forma financial information to U.S. GAAP. However, if a foreign private issuer using IFRS acquires a domestic company using U.S. GAAP, a partial reconciliation to IFRS is required so that the foreign company, acquiror, is able to present pro forma financial information using IFRS. Similarly, a partial reconciliation is required when a U.S. company using U.S. GAAP acquires a foreign company using IFRS.

The SEC also proposed conforming amendments to the references to U.S. GAAP reconciliation set forth in Form F-4 (registration statements of foreign private issuers issued in certain business combinations); Form S-4 (registration statement for securities of domestic issuers issued in business combination transactions); and Rule 701 under the Securities Act (currently requiring a company to reconcile its financial statements to U.S. GAAP when it sells more than \$5 million of securities per 12 months to its employees).

The proposed amendments will also effectively allow foreign private issuers to file financial statements prepared under IFRS as published by the IASB in the context of Schedule TO (tender offer statements) and Schedule 13E-3 filings (transaction statements under Section 13(e) of the Exchange Act); and filings under the Multijurisdictional Disclosure System (“MJDS”) by certain Canadian foreign private issuers.

#### IV. SEC Seeking Comments on Proposed Amendments

The SEC is seeking comments from interested parties on the proposed amendments, including comments on the question of whether U.S. investors would be able to understand and use financial statements prepared in accordance with IRFS as published by the IASB without a U.S. GAAP reconciliation.

The SEC is also seeking comments on the possibility of shortening the deadline for filing annual reports on Form 20-F.

Comments are due on September 24, 2007.

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This memorandum is not intended to provide legal advice with respect to any particular situation and no legal or business decision should be based solely on its content. Questions concerning issues addressed in this memorandum should be directed to any member of the Paul Weiss Securities Group, including:

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