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SEC Adopts Amendments to Foreign Issuer Reporting Requirements

Last week, the SEC published final rules[1] amending certain rules applicable to foreign private issuers under the U.S. Securities Exchange Act of 1934 (the "Exchange Act"). The amendments are part of the SEC's recent initiatives to modernize the reporting requirements under the Exchange Act in the wake of the ongoing globalization of securities markets, and aim to enhance disclosure provided by foreign private issuers in response to prior changes in filing requirements for U.S. domestic companies, changes in investor expectations and market practices, advances in technology, developments in foreign filing requirements and changes in other areas of SEC regulation.

The changes include:

- ***Annual evaluation of foreign private issuer status.*** Foreign issuers will be able to assess their status as "foreign private issuers" once a year on the last business day of their second fiscal quarter (rather than on a continuous basis, as was formerly required). If a foreign issuer determines that it no longer qualifies as a foreign private issuer on the last business day of its second fiscal quarter, it must comply with the rules applicable to domestic companies beginning on the first day of the fiscal year following such determination.

- ***Four-month Form 20-F filing deadline.*** Following a three-year transition period ending December 15, 2011 (which is one year longer than the SEC's initial proposal), the filing deadline for annual reports on Form 20-F will be accelerated from six months to four months after the issuer's fiscal year-end. This provision does not distinguish among types of issuers (*i.e.*, accelerated and large accelerated, and other, filers).

- ***Form 20-F, Items 17 and 18.*** The SEC has eliminated an instruction to Item 17 that permits foreign private issuers to omit segment data from their U.S. GAAP financial statements. In addition, after a three-year transition period ending December 15, 2011 (which is two years longer than the SEC's initial proposal), the SEC is eliminating such accommodation provided in Item 17 of Form 20-F, thereby requiring foreign private issuers that currently prepare financial statements in accordance with Item 17 to provide a U.S. GAAP reconciliation (if such reconciliation is required) pursuant to Item 18 of Form 20-F (for registration statements and annual reports).

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1 The final release is available at http://www.sec.gov/rules/final/2008/33-8959.pdf.

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- ***Rule 13e-3 "Going Private" Transactions.*** The SEC has amended Rule 13e-3, which imposes disclosure and other requirements on "going private" transactions, to add to the list of transactions that trigger the rules transactions that have the reasonable likelihood or purpose of causing termination of reporting obligations under rules adopted in 2007 facilitating deregistration by foreign private issuers.

- ***Additional Form 20-F disclosure.*** Form 20-F has been amended to require disclosure concerning
  - changes in, and disagreements with, the foreign private issuer's certifying accountants (effective for its first fiscal year ending on or after December 15, 2009);
  - fees, payments and other charges relating to ADRs (effective for its first fiscal year ending on or after December 15, 2009); and
  - significant differences in the foreign private issuer's corporate governance practices as compared to U.S. issuers (effective for its first fiscal year ending on or after December 15, 2008).

The SEC did not adopt rule changes that would have imposed on foreign private issuers an obligation to provide standalone financial statements and pro forma financial information in annual reports for highly significant acquisitions.

Annual Test for Foreign Private Issuer Status

The determination of whether a foreign company filing a registration statement or annual report with the SEC qualifies (or continues to qualify) as a "foreign private issuer" is important given that foreign private issuers can take advantage of various accommodations and exemptions under the Exchange Act.[2] Under Exchange Act Rule 3b-4, a foreign issuer can lose its "foreign private issuer" status at any time, if:

- more than 50% of the issuer's outstanding voting securities are directly or indirectly held of record by U.S. residents; ***and***

- (a) the majority of the executive officers or directors are U.S. citizens or residents, (b) more than 50% of the assets of the issuer are located in the United States, ***or*** (c) the business of the issuer is administered principally in the United States.

As a result, under current rules, there can be uncertainty as to the applicable requirements for foreign private issuers that have close to 50% of their outstanding voting securities held of record by U.S. residents.

To provide greater certainty to both issuers and investors as to the status of foreign private issuers within a given period of time, the amendments permit foreign private issuers to assess their status once a year. Specifically, reporting foreign issuers, including Canadian issuers relying upon the multi-jurisdictional disclosure system ("MJDS"), will be permitted to assess their status on the last business day of their second fiscal quarter. Canadian issuers that file annual reports on Form

[2] For example, foreign private issuers are exempt from the SEC's proxy rules and from the insider stock trading reports and short-swing profit recovery provisions under the Exchange Act. They also provide interim reports on the basis of home country regulatory practices, and executive compensation disclosure on an aggregate basis if the information is reported on such a basis in the issuer's home country.

40-F, however, will additionally need to test their eligibility under the other requirements of Form 40-F (such as public float) at the end of its fiscal year.

Under the amendments, if a foreign issuer determines that it no longer qualifies as a foreign private issuer on the last business day of its second fiscal quarter, it would be required to comply with the reporting requirements and use the forms prescribed for U.S. domestic issuers beginning on the first day of the fiscal year following the determination date. On the other hand, a reporting company that qualifies as a foreign private issuer may take advantage of the foreign private issuer accommodations, including forms and reporting requirements, on the determination date on which it establishes its eligibility as a foreign private issuer.

Accelerating the Reporting Deadline for Form 20-F Annual Reports to Four Months

The SEC has accelerated the due date for annual reports filed on Form 20-F, from six months to four months after the fiscal year-end for all foreign private issuers.[3] A three-year transition period has been provided, as a result of which the accelerated filing deadline will become effective for annual reports on Form 20-F for fiscal years ending on or after December 15, 2011.

Segment Data Disclosure

Prior to the amendments, foreign private issuers that presented financial statements otherwise fully in compliance with U.S. GAAP could omit segment data from their financial statements under Item 17 of Form 20-F, and could also have a qualified U.S. GAAP audit reports as a result of this omission. The SEC noted that approximately five foreign private issuers have relied on this accommodation in the past few years and has, therefore, eliminated it. Foreign private issuers will be required to comply with this amendment beginning with their first fiscal year ending on or after December 15, 2009.

Exchange Act Rule 13e-3

The SEC has amended Exchange Act Rule 13e-3, which governs "going private" transactions, to reflect the amended bases for deregistration and termination of reporting obligations applicable to foreign private issuers (Exchange Act Rule 12h-6, which established an alternate a deregistration test based on a comparison of U.S. and worldwide ADTV (in addition to the 300-U.S. holder test). Under the amended rule, Rule 13e-3 can be triggered when a foreign private issuer engages in a transaction that has a reasonable likelihood, or purpose of causing, the issuer to:

- deregister its securities or terminate its reporting obligations under Exchange Act Rule 12h-6 (*i.e.*, where the U.S. ADTV is not greater than 5% of the worldwide ADTV, or the securities are held by less than 300 U.S. residents or less than 300 persons worldwide); or

- suspend its Exchange Act Section 15(d) reporting obligations under Rule 12h-3 (*i.e.*, the securities are held by less then 300 persons, or by less than 500 persons, where the

[3] The SEC had originally proposed to accelerate the filing deadline for Form 20-F annual reports based on filing status (*i.e.*, the deadline would vary depending on whether a foreign private issuer was a large accelerated filer, an accelerated filer, or other filer).

total assets of such issuer have not exceeded $10 million on the last day of each of its three most recent fiscal years).

Requiring Item 18 Reconciliation in Annual Reports and Registration Statements Filed on Form 20-F

If a foreign private issuer prepares its financial statements and schedules in accordance with a basis of accounting other than U.S. GAAP, or IFRS as issued by the IASB, then the issuer must include a reconciliation to U.S. GAAP. Prior to the amendments, if a foreign private issuer qualified to use Item 17 of Form 20-F for financial statement requirements, this reconciliation was partial and only required the inclusion of a narrative discussion of reconciling differences, a reconciliation of net income for each year and any interim periods presented, a reconciliation of major balance sheet captions for each year and any interim periods, and a reconciliation of cash flows for each year and any interim periods. On the other hand, under Item 18 of Form 20-F, all other foreign private issuers were required to provide all information provided by U.S. GAAP and Regulation S-X, in addition to the reconciling information for the line items specified in Item 17.

The amendment has eliminated the availability of Item 17 for foreign private issuers that:

- are only listing a class of securities on an exchange, or only registering a class of securities under Exchange Act Section 12(g), without conducting a public offering;
- file annual reports on Form 20-F; or
- are undertaking certain non-capital raising offerings, such as an offerings pursuant to reinvestment plans, offerings upon the conversion of securities, or offerings of investment grade securities.

As a result, foreign private issuers that prepare disclosure for any of the above will be required to provide Item 18 information (which means a reconciliation that includes the footnote disclosures required by U.S. GAAP and Regulation S-X).

Item 17 disclosure will, however, continue to be available for:

- Canadian MJDS filers; and
- third-party financial statements of non-registrants that are required to be included in a foreign or domestic issuer's registration statement, annual report or other Exchange Act report (such as significant acquired businesses under Rule 3-05 of Regulation S-X, significant equity method investees under Rule 3-09 of Regulation S-X, entities whose securities are pledged as collateral under Rule 3-16 of Regulation S-X, and exempt guarantors under Rule 3-10(i) of Regulation S-X).

Additional Form 20-F disclosure

Disclosure about Change in a Registrant's Certifying Accountant

The amendments to Form 20-F require new disclosure relating to changes in, and disagreements with, the foreign private issuer's certifying accountant. The SEC believes that the disclosure requirement addresses potential "opinion shopping" situations by issuers. "Opinion shopping" generally refers to the search for an auditor that is willing to support a proposed

accounting treatment that is designed to help a company achieve its reporting objectives, even though that treatment could frustrate reliable reporting.

The Form 20-F disclosure amendments aim to require substantially the same types of disclosures currently provided by U.S. domestic issuers about changes in, and disagreements with, their certifying accountant, including disclosure of:

- whether an independent accountant that was previously engaged as the principal accountant to audit the issuer's financial statements, or a significant subsidiary on which the accountant expressed reliance in its report, has resigned, declined to stand for re-election, or was dismissed;

- any disagreements or reportable events that occurred within the issuer's latest two fiscal years and any interim period preceding the change of accountant; and

- whether, during the fiscal year in which the change of accountants took place or during the subsequent year, the issuer had similar material transactions to those that led to the disagreements with the former accountants, and whether such transactions were accounted for or disclosed in a manner different from that which the former accountants would have concluded was required. (If so, the issuer would be required to disclose the existence and nature of the disagreement or reportable event, and also disclose the effect on the financial statements if the method that would have been required by the former accountants had been followed.).

In addition, a letter from the former accountant will need to be filed as an exhibit to the relevant form, stating whether the former accountant agrees with the statements made by the issuer and, if not, stating the respects in which it does not agree.

The disclosure would be required in annual reports on Form 20-F, as well as registration statements filed on Forms 20-F, F-1, F-3 and F-4.

Annual Disclosure about ADR Fees and Payments

Noting that current disclosure about fees and other payments made by ADR holders are often generic (*i.e.*, merely providing maximums paid on the deposit and withdrawal of the securities underlying the ADRs), the SEC has adopted amendments to enhance such disclosure by requiring disclosure under Item 12.D.3 of Form 20-F of:

- ADR fees on an annual basis, including any annual fee for general depositary services; and

- any payments made by depositaries to the foreign issuers whose securities underlie the ADRs.

Issuers must make these disclosures on a per payment basis rather than on an aggregate basis. The above disclosure would be required in any registration statement on Form 20-F that is filed for the deposited securities, as well as in each annual report on Form 20-F if the foreign private issuer has a sponsored ADR facility. These amendments do not affect the fact that disclosure of those fees would also be made in the form of ADR included as part of a deposit agreement (and filed as an exhibit to a Form F-6).

Concerns over disclosure of incentive payments have been addressed through a delayed implementation period (annual report for the first fiscal year ending on or after December 15, 2009), thus allowing issuers and their depositaries to make appropriate contractual arrangements, if appropriate.

Disclosure about Differences in Corporate Governance Practices

Foreign private issuers are exempt from many of the corporate governance requirements prescribed by U.S. securities exchanges when their home country practices differ from that of U.S. domestic companies. As a condition to the exemption, foreign private issuers are required to disclose the significant ways in which their corporate governance practices differ from those followed by U.S. domestic companies under the relevant exchange's listing standards.

To consolidate this corporate governance disclosure in a single location rather than creating options to report the information either in annual reports and/or on websites, new Item 16G requires the disclosure to be included in the annual report.

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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.