Paul|Weiss

April 6, 2004

# Update: Rule 12g3-2(b) Exemption from SEC Reporting

The *Financial Times* reported today that a UK company could inadvertently find itself subject to the reporting requirements of the US Securities and Exchange Commission or face other sanctions by reason of the belated discovery of American Depositary Receipts issued some years ago under an unsponsored program. The issue came to light when the company sought an exemption from the SEC reporting requirements and found that the number of holders of its securities (in this case, ADRs representing ordinary shares) exceeded the maximum number permitted for a company requesting such relief.

The FT article was referring to a procedure whereby non-US companies can obtain an exemption from the reporting requirements of the US securities laws if at the time the exemption is requested the company has fewer than 300 shareholders resident in the United States. The 300-holder limit is the same limit that triggers an SEC reporting obligation. The essence of the relief is that prior to the time a company reaches the reporting threshold, it can seek relief, which will remain effective so long as the company does not take active affirmative steps to US enter the capital markets through a listing or a public offering. The relief is intended to protect companies whose US share ownership levels increase through no effort on their part (such as an unsponsored ADR program) or through activities that fall short of an active marketing effort (such as a so-called "Level I ADR program" or an non-public offering in the United States, such as under Rule 144A).

This memorandum provides a brief overview of the exemption and the advantages of seeking and maintaining the exemption.

**The SEC Registration Obligation**

Generally speaking, any company—whether US or non-US—that wishes to offer or sell its securities in a public offering in the United States must register the proposed public offering under, and follow the other rules in, the Securities Act of 1933 (the "Securities Act"). Any company that wishes to list its securities on a national securities exchange (such as the NYSE) or on the Nasdaq Stock Market must register those securities under the Securities Exchange Act of 1934 (the "Exchange Act"). Additionally, subject to limited exceptions discussed below, a non-US issuer that effects a public offering of securities in the United States (including by way of a registered exchange offer), even if those securities are not listed on an exchange or quoted on Nasdaq, will by virtue of Section 15(d) of the Exchange Act be subject to reporting requirements (including SEC rules adopted in connection with the Sarbanes-Oxley Act), at least during the year in which such offering occurs, and thereafter if the non-US issuer has 300 or more US securityholders (of any single class).

The Exchange Act also imposes a separate registration requirement on companies whose equity securities are widely-held in the United States, even if the securities are not listed on a US

1285 Avenue of the Americas
New York, New York 10019-6064
(212) 373-3000

1615 L Street, NW
Washington, DC 20036-5694
(202) 223-7300

Alder Castle, 10 Noble Street
London EC2V 7JU England
(44-20) 7367 1600

2, rue du Faubourg Saint-Honoré
75008 Paris, France
(33-1) 53.43.14.14

Fukoku Seimei Building 2nd Floor
2-2, Uchisawaicho 2-chome
Chiyoda-ku, Tokyo 100, Japan
(81-3) 3597-8120

Oriental Plaza, Tower E3, Ste.1205
No. 1, East Chang An Avenue
Beijing 100738, People's Republic of China
(86-10) 8518-2766

12th Fl., Hong Kong Club Building
3A Chater Road, Central
Hong Kong
(852) 2536-9933

exchange. In general, under the Exchange Act, if an issuer's equity securities are held of record by 500 or more persons worldwide (and more than 300 in the United States) and the issuer has assets exceeding US$10 million, the issuer must register the class of securities with the SEC and thereafter comply with US reporting requirements.

**The Information-Supplying Exemption**

Non-US issuers may, however, obtain an exemption from this registration and reporting requirement under the so-called "information-supplying" exemption of Rule 12g3-2(b). Under this exemption, such non-US issuers may provide to the SEC copies of reports required to be filed in their home country in lieu of reports required to be filed under the Exchange Act. This exemption is available for any class of securities issued by a non-US issuer if that class has fewer than 300 holders resident in the United States (notwithstanding that there are 500 or more holders worldwide) ***at the time of the application***. For purposes of determining whether securities are held by fewer than 300 US residents, securities held of record by a broker, dealer, bank (or a nominee for any of the foregoing) for the accounts of customers resident in the United States are counted as held in the United States by the number of separate accounts for which the securities are held.

None of the information furnished to the SEC under Rule 12g3-2(b) is considered to be "filed" with the SEC or otherwise subject to the liabilities of Section 18 of the Exchange Act, which imposes liability for false and misleading statements made in any application, report or document "filed" under the Exchange Act. The submitting company may be subject to liability for fraudulent mistatements or omissions.

The Rule 12g3-2(b) exemption is not available if the issuer's securities are listed on a US national securities exchange (such as the NYSE) or quoted on Nasdaq, or if the non-US issuer has made or is making a public offering of securities in the United States. The exemption is also not available if at the time the exemption is applied for, the issuer would otherwise be required to register under the Exchange Act. Thus, any issuer contemplating applying for an exemption should do so, for example, before it has more than 300 holders resident in the United States, calculated as described above on a "look-through" basis.

To obtain an exemption under Rule 12g3-2(b), an issuer must furnish to the SEC whatever information, since the beginning of its last fiscal year, the issuer (i) has made or is required to make public pursuant to the law of the jurisdiction of its domicile or in which it is incorporated or organized, (ii) has filed or is required to file with the local stock exchange on which its securities are traded and which was made public by such exchange or (iii) has distributed or is required to distribute to its securityholders. Once the exemption has been granted, any such information made public during each subsequent fiscal year must be furnished to the SEC "promptly" after it is made public.

**Advantages of Seeking the Exemption**

Issuers may want to seek an exemption under Rule 12g3-2(b) for a variety of reasons, including:

- An issuer that in the foreseeable future is likely to have 300 or more securityholders in the United States but does not have securities listed on a

national securities exchange or quoted on Nasdaq would be well advised to obtain the exemption. Without the exemption, upon reaching 300 or more securityholders in the United States, the issuer would be obligated to register under the Exchange Act and thus file period reports with the SEC, whether or not it has assets in the United States, has actively sought to build up its shareholder base in the United States or has any other connection with the United States.

- The issuer wishes to establish a so-called Level I ADR program (which is an over-the-counter program that falls short of a formal listing, but permits US residents to trade in securities of the issuer in dollars in the US settlement system; the establishment of the program does not trigger reporting obligations or compliance with US rules, including Sarbanes-Oxley Act requirements).

- The issuer wishes to undertake an offering of securities into the United States under Rule 144A, either as a single targeted offering into the United States or as part of a global offering with a US tranche (an advantage of the Rule 144A route is that it provides a measure of liquidity (as the securities can be freely traded among "qualified institutional buyers") without the need for SEC registration or SEC reporting).

The exemption is easy to obtain and easy to maintain. The information supplied to the SEC is not deemed "filed" for liability purposes. The scope of information that is supplied is dictated by local requirements and no additional information need be generated (e.g., US GAAP financial statements). The exemption does not trigger application of US corporate governance rules (including the Sarbanes-Oxley Act).

**What Should Companies Do?**

The FT article serves as a useful reminder that non-US issuers should be mindful of the levels of share ownership by US residents. As the markets continue to become more global, the likelihood that a non-US company could find itself with more that 300 shareholders resident in the United States increases. Non-US issuers should also take steps to confirm that their securities are not traded in ADR form through an unsponsored program (which are rarely set up these days, but programs dating back 15-20 years might still exist).

Obtaining the reporting exemption could serve to protect the company were interest in its securities among US residents to increase as well as to facilitate subsequent entry into the US capital markets. As is highlighted in the case reported today in the FT, what is critical is that the request for the exemption be made prior to the time the company crosses the 300-holder threshold. Non-US companies would be well-advised to consider the issue before it gets too close to the threshold.

* * * *

Should you have any questions concerning the Rule 12g3-2(b) exemption, please do not hesitate to call any of the following members of the Paul, Weiss Securities Group. In addition, memoranda on related topics may be accessed under Securities Group publications on our web site (www.paulweiss.com).

| | | | |
|---|---|---|---|
| Mark S. Bergman | (44 20) 7367-1601 | Andrew J. Foley | (1) 212-373-3078 |
| David K. Lakhdhir | (44 20) 7367-1602 | Edwin S. Maynard | (1) 212-373-3024 |
| Gábor Molnár | (44 20) 7367-1605 | Raphael M. Russo | (1) 212-373-3309 |
| Tong Yu | (81 3) 3597-6306 | | |