SEC Reproposes Rules Easing Deregistration by Foreign Private Issuers

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The Securities and Exchange Commission has reproposed new rules[1] that are designed to make it easier for foreign private issuers to deregister their securities and terminate their corresponding reporting obligations under the U.S. Securities Exchange Act of 1934.

The new rules will allow a foreign private issuer to deregister a class of its equity securities if the U.S. trading volume for that class of equity security has been not greater than 5% of its trading volume in its primary trading market during a recent twelve-month period, and certain other conditions are met. A foreign private issuer currently must establish that there are fewer than 300 U.S. holders of a class of securities to deregister.

The new rules will also allow a foreign private issuer to terminate, and not merely suspend, its SEC reporting obligations if it satisfies the conditions of the rules. A foreign private issuer that has issued securities in a registered public offering in the United States currently may only suspend its reporting obligations and must count its U.S. security holders at the beginning of each subsequent fiscal year to determine whether its reporting obligations will resume that year.

The new rules will make it easier for foreign private issuers to claim the "Rule 12g3-2(b) exemption" from registration and to comply with the ongoing requirements of the exemption; modify the method of counting U.S. security holders; introduce notice and other procedural changes to the deregistration process; and address other issues relating to deregistration.

The public comment period expires on February 12, 2007. The SEC currently anticipates that the proposed rules will be in effect before March 31, 2007. If the SEC meets this deadline, eligible foreign private issuers with fiscal years ending in December that promptly make a filing claiming the benefits of the new rules may avoid the need to file an annual report for 2006.

BACKGROUND

The U.S. securities regulatory system makes it difficult for a non-U.S. company to exit the SEC reporting regime, even when U.S. investor interest in the company's securities is low. This issue became particularly acute in the wake of the Sarbanes–Oxley legislation, which induced many foreign companies to avoid the U.S. public securities markets out of fear of assuming higher regulatory burdens for an indefinite period of time.

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1 SEC Release No. 34-55005 dated December 22, 2006. The principal substantive changes to the deregistration process are set out in proposed Rule 12h-6.

To address this issue and encourage foreign companies to participate in the U.S. public capital markets, the SEC originally proposed new rules in December 2005 to simplify the exit process. However, this proposal met with dissatisfaction, particularly with respect to the proposed benchmarks for measuring investor interest. The SEC has now modified its proposal to take account of these concerns. The modified version of the proposed rules was released on December 22, 2006.

DEREGISTRATION OF EQUITY SECURITIES

Under the proposed rules, a foreign private issuer will be able to deregister a class of equity securities and terminate the SEC reporting obligations arising from registration of that class by meeting the following conditions:

- *Quantitative benchmark condition* - based on either the new "trading volume" test or the existing test based on the number of U.S. resident record holders of its shares in the United States.

- *Prior reporting condition* - stipulating that the foreign private issuer must have had SEC reporting obligations for at least one year before deregistration, must have filed at least one annual report, and must be current in its reporting obligations.

- *Dormancy condition* - prohibiting sales of the foreign private issuer's securities in the United States in a registered public offering during the year before deregistration.

- F*oreign listing condition* - requiring that the foreign private issuer has maintained for at least one year a listing of the equity securities on a foreign exchange that either singly or with one other foreign exchange constitutes the primary trading market for the security.

A foreign private issuer will certify its eligibility for deregistration by filing a new form called a Form 15F.

Quantitative Benchmark

Proposed Rule 12h-6 will offer foreign private issuers the choice of two tests to demonstrate low U.S. market interest in a class of equity securities that it seeks to deregister: the trading volume test; and a revamped version of the existing record holder test.

Trading Volume Test

To meet the trading volume test, a foreign private issuer will have to demonstrate that the average daily trading volume (the "ADTV") of the class of equity securities in the United States has been 5% or less of the ADTV of that equity security in its "primary trading market" during a recent twelve-month period. The measurement of an equity security's ADTV in the United States must take into account all U.S. trading activity and not just activity on a securities exchange. The foreign private

issuer will be able to use information that is publicly available from reliable sources to measure ADTV.

The "primary trading market" for a class of securities (whether equity or debt) is the foreign jurisdiction in which at least 55% of the trading in the security took place in, on or through the facilities of a securities market during a recent twelve month period. Two foreign jurisdictions may together constitute a foreign private issuer's primary trading market if their aggregated trading volume reaches the 55% mark, but only if the trading market in at least one of the two foreign jurisdictions is larger than the U.S. trading market for the same class of the issuer's securities.

In proposing the trading volume test, the SEC was concerned that issuers could cause trading volumes in the United States to drop, thereby making it easier to deregister, by taking actions detrimental to shareholders. Accordingly, a foreign private issuer that delists a class of equity securities from a U.S. national securities exchange or automated inter-dealer quotation system will be subject to a one-year waiting period before it may deregister unless it satisfied the trading volume test on the date of its delisting and over the preceding twelve months. In addition, if an equity security is traded as an American Depositary Receipt ("ADR"), through a sponsored ADR facility, a foreign private issuer will have to wait twelve months after terminating the ADR facility before it could rely on the trading volume test.

Record Holder Test

To meet the record holder test, a foreign private issuer will have to demonstrate that there are fewer than 300 record holders of the class of securities either on a worldwide basis or who are U.S. residents. To determine the number of record holders who are U.S. residents, a foreign private issuer will be able to use a less rigorous version of the "look through" counting method found in the existing rules. The inquiry will be limited to brokers, banks and other nominees located in the United States, in the foreign private issuer's jurisdiction of legal formation and, if different, in the jurisdiction(s) constituting the foreign private issuer's primary trading market.

In measuring the number of record holders, a foreign private issuer could rely on a presumption that if, after reasonable inquiry, it is unable without unreasonable effort to obtain information about the amount of securities held by nominees for the accounts of customers resident in the United States, it may assume that the customers are the residents of the jurisdiction in which the nominee has its principal place of business.

The foreign private issuer will also be able to rely in good faith on the assistance of an independent information services provider that in the regular course of business assists issuers in determining the number of, and collecting other information concerning, their security holders.

Reporting Condition

On the date it files its Form 15F, a foreign private issuer must have been subject to SEC reporting obligations for at least twelve months, must be current in all reporting obligations and must have filed at least one annual report (e.g., 20-F or 10-K).

Dormancy Condition

For twelve months preceding the filing of Form 15F, the foreign private issuer's securities have not been sold in the United States in a registered public offering under the Securities Act other than:

- to the foreign private issuer's employees;
- by selling security holders in non-underwritten offerings;
- upon the exercise of outstanding rights granted by the foreign private issuer if the rights are granted pro rata to all existing security holders of the class of securities to which rights attach;
- pursuant to a dividend or interest reinvestment plan; or
- upon the conversion of outstanding convertible securities or upon the exercise of outstanding transferable warrants of the foreign private issuer.

The above exceptions do not include securities issued pursuant to a standby underwritten offering or other similar arrangement in the United States.

The dormancy condition is designed to prevent a foreign private issuer from deregistering securities shortly after have accessed the U.S. public capital markets. However, the condition will not preclude unregistered sales of securities in the United States, including Rule 144A offerings or in Section 4(2) or Regulation D private placements in addition to certain other classes of unregistered offerings.

Foreign Listing Condition

For at least the twelve months preceding the foreign private issuer's filing of its Form 15F, the class of equity securities must have had a primary trading market and must have been listed on an exchange in its primary trading market. The purpose of the foreign listing condition is to ensure that a foreign private issuer will be subject to regulatory oversight outside of the United States after deregistering its securities and that U.S. investors will still receive a minimum level of information about the company as a result of non-U.S. disclosure requirements.

DEREGISTRATION OF DEBT SECURITIES

For those non-U.S. companies subject to SEC reporting obligations by virtue of having publicly offered a class of debt securities, the most important change introduced by the proposed rules is the ability to terminate, and not merely suspend, those SEC reporting obligations. In addition, the modified "look through" method of counting U.S. holders will make the determination of U.S. market interest easier for all foreign private issuers with registered debt securities. The benchmark for measuring U.S. market interest will remain the same as under existing rules: fewer than 300 record holders of the debt security in the United States. Under the proposed rules, a foreign private issuer will be entitled to terminate its SEC reporting obligations with regard to the class of debt securities if it can satisfy the 300 record holder test, and has filed or furnished all required SEC reports, including at least one annual report.

CHANGES TO METHOD OF COUNTING RECORD HOLDERS

As mentioned above, the proposed rules will modify the manner in which a foreign private issuer must count holders of its securities for purposes of applying the 300 record holder benchmark (whether as the alternative benchmark for an equity securities deregistration, or as the benchmark for a debt securities deregistration). Instead of "looking through" brokers, banks and nominees on a worldwide basis to determine the number of U.S. security holders, the foreign private issuer will be able to limit its inquiry to brokers, banks and other nominees located in the United States, in the issuer's jurisdiction of incorporation, legal organization or establishment and, if different, in the jurisdiction(s) of its primary trading market.

If a foreign private issuer aggregates two foreign jurisdictions as its primary trading market for the purpose of meeting the foreign listing condition mentioned above, the issuer will have to look through nominee accounts in both jurisdictions, as well as its jurisdiction of organization and the United States.

If, after reasonable inquiry, an issuer will be unable without unreasonable effort to obtain information about U.S. ownership, it will be able to assume that the owners are the residents of the jurisdiction in which their nominees have their principal places of business.

AMENDMENTS TO RULE 12G3-2(B) EXEMPTION

Rule 12g3-2(b) currently provides an exemption for foreign private issuers from the SEC reporting requirements that will otherwise apply if the issuer were to have more than 300 record holders of its equity securities in the United States. The exemption currently is not available to foreign private issuers that have made a registered public offering in the United States or that have otherwise been subject to SEC reporting requirements within the previous 18 months. One of the conditions of the exemption is that issuers file with the SEC on an on-going basis their "home country" reports.

The proposed rules will effect several important changes to the Rule 12g3-2(b) exemption:

- Foreign private issuers will be able to rely on the 12g3-2(b) reporting exemption with respect to an equity security *immediately* upon deregistration, instead of waiting 18 months after deregistration.

- The 12g3-2(b) exemption will be available to foreign private issuers even though they had become subject to SEC reporting obligations because of a registered public offering in the United States.

- A foreign private issuer must publish home country reports in English on its website or through an electronic delivery system generally available to the public in its primary trading market. (Under the current rules, all such required information must be submitted to the SEC in hard copy.)

DEREGISTRATION PROCESS

Form 15F Disclosure

Under the proposed rules, a foreign private issuer will file a Form 15F to establish its eligibility to deregister a class of security. By signing and filing Form 15F, the foreign private issuer will be certifying that:

- it meets all of the conditions for termination of SEC reporting specified in Rule 12h-6; and

- there are no classes of securities other than those that are the subject of the Form 15F for which the foreign private issuer has SEC reporting obligations.

Form 15F will also require a foreign private issuer to provide information about the decision to terminate its SEC reporting requirements including its reporting history, its last sale of registered securities, and, as applicable, the primary trading market, trading volume data and number of record holders of the subject class of securities.

Post-Filing Waiting Period

As with Form 15 under the current rules, the filing of a Form 15F will immediately suspend a foreign private issuer's SEC reporting obligations. The SEC will then have 90 days to object to the filing. In the absence of an objection, the class of securities will automatically become deregistered and the related reporting obligations will be terminated. If, however, the SEC rejects the Form 15F or the foreign private issuer withdraws it, the issuer will then have 60 days to file or submit all reports that it will have been required to file or submit had it not filed a Form 15F.

After filing its Form 15F, a foreign private issuer will have no continuing duty to make further inquiries to prove its eligibility to deregister, including with respect to the trading volume or

ownership of the subject class of securities. However, if, during the 90-day waiting period, the foreign private issuer has actual knowledge of information that causes it reasonably to believe that at the date of filing it did not satisfy the trading volume test or the record holder test, as applicable, or otherwise was not qualified to deregister under Rule 12h-6, the foreign private issuer will have to withdraw its Form 15F.

Notice

Under Rule 12h-6, a foreign private issuer will have to publish, either before or on the date that it files its Form 15F, a notice in the United States that discloses its intent to terminate its SEC reporting obligations. The foreign private issuer will have to publish the notice, such as a press release, through a means reasonably designed to provide broad dissemination of the information to the public in the United States. The foreign private issuer also will be required to submit a copy of the notice to the SEC, either under the cover of a Form 6-K before or at the time of filing of the Form 15F, or as an exhibit to the Form 15F.

OTHER CHANGES

Previous Filers of Form 15

Proposed Rule 12h-6 will permit foreign private issuers that have already suspended their SEC reporting obligations by filing a Form 15 under the existing rules to terminate permanently their SEC reporting obligations and to rely on the amended Rule 12g3-2 exemption. A prior Form 15 filer will have to meet the following conditions in order to obtain these benefits:

- It must file Form 15F;
- It must not be subject to an obligation to register a class of securities under Section 12(g) of the Exchange Act or file reports under section 15(d); and
- With respect to a class of equity securities, it will have to meet the foreign listing condition described above.

Unlike other foreign private issuers, prior Form 15 filers will not have to meet any quantitative benchmarks or satisfy prior reporting or dormancy requirements to deregister under the proposed rules. The public notice requirement will also not apply to prior Form 15 filers.

Successor Issuers

Proposed Rule 12h-6 will extend the right to deregister securities to a foreign private issuer that has succeeded to the SEC reporting obligations of another issuer following a merger, consolidation, exchange of securities, acquisition of assets or similar transaction. The successor may terminate its inherited reporting obligations with respect to a class of equity securities if it meets the prior reporting, foreign listing, and quantitative benchmark conditions described above. A successor may

terminate its inherited reporting obligation with respect to a class of debt securities if it meets all of the debt security deregistration requirements otherwise applicable to foreign private issuers, as described above. For both equity and debt securities, the one-year prior reporting condition will be deemed satisfied for a successor if it has been satisfied by the predecessor issuer.

This memorandum is for general informational purposes and should not be regarded as legal advice. Please contact your relationship partner if we can be of assistance regarding these important developments. The names and office locations of all of our partners, as well as additional memoranda regarding recent securities law developments, can be obtained from our website, www.simpsonthacher.com.

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