Foreign Private Issuers: Overview of Securities Law Requirements

Public Company Advisory Practice

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GOODWIN

Foreign Private Issuers: Overview of Securities Law Requirements

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Rationale for Foreign Private Issuer Accommodations

- Encourage listing on a U.S. market
- Facilitate investment by U.S. investors in foreign companies
- Reduce regulatory arbitrage
- Reduce cost of raising capital across borders and encourage free flow of capital across borders
- Comity considerations with home country
- U.S. investors can invest directly abroad (e.g., on the London Stock Exchange), so U.S. regulators consider it preferable to provide some added U.S. investor protection rather than none

Benefits of being a Foreign Private Issuer

- Accommodations in securities registration process and ongoing public reporting requirements:
  - Ability to use particular registration and reporting forms specific to foreign private issuers.
  - Ability to use U.S. GAAP, International Financial Reporting Standards (IFRS) or home country accounting standards reconciled to U.S. GAAP.
  - More time to file Form 20-F Annual Report (120 days after fiscal-year end).
  - More limited executive compensation disclosures.
  - Quarterly reporting on Form 10-Q and current reporting on Form 8-K are not required.
  - Financial information goes “stale” more slowly.
  - Exempt from proxy rules, Regulation FD, and Section 16 reporting and short-swing profit liability.

Benefits of being a Foreign Private Issuer

- Foreign private issuers may elect to use the same registration and reporting forms that domestic companies use, but in making such an election the company must comply with all of the requirements of the domestic company forms, absent a specified accommodation.
- Foreign private issuers that voluntarily file on domestic forms may file financial statements prepared under:
  - "Home country" GAAP and provide a reconciliation to U.S. GAAP, or
  - IFRS as issued by the IASB without reconciliation to U.S. GAAP.
  - In both cases the filings should prominently disclose that the company meets the foreign private issuer definition but is voluntarily filing on domestic forms.
- If an FPI elects to use the forms for domestic issuers, it should assess whether it qualifies as a smaller reporting company (SRC). An FPI that qualifies as an SRC may take advantage of the scaled disclosure requirements for SRCs. However, companies that elect to avail themselves of the scaled disclosure regime for SRCs must use the forms for domestic issuers, and present their financial statements in accordance with U.S. GAAP.
- Stock exchange rules permit compliance with "home country" corporate governance standards.

Definition of “Foreign Private Issuer”

- A company qualifies for “foreign private issuer”(FPI) status if it is incorporated/organized outside the U.S. and 50% or less of its outstanding voting securities are held by U.S. residents; or
  - If more than 50% of its outstanding voting securities are directly or indirectly owned of record by U.S. residents, then none of the following three circumstances may apply:
    - A majority of its directors or executive officers are U.S. citizens or residents;
    - More than 50% of its assets are located in the United States; or
    - Its business is principally administered in the United States (primarily directed or controlled).
  - If an issuer has two boards of directors, the determination is made with respect to the board that performs the functions most closely related to those undertaken by a U.S.-style board of directors. If those functions are divided between both boards, the issuer may aggregate the members of both boards for purposes of calculating the majority.
  - When determining ownership, one must "look through" nominee accounts held in the U.S., the company’s home jurisdiction, and the jurisdiction of its principal trading market if different from its home jurisdiction
- New registrants must test their status as of a date within 30 days of initial filing of a registration statement with the SEC and, thereafter, companies must test annually on the last business day of the second fiscal quarter.

Definition of “Foreign Private Issuer”

- **Shareholder test**
  - *Reasonable inquiry* – If issuer is unable to obtain information about the amount of shares represented by accounts of customers in the U.S., it may assume that the customers are residents of the jurisdiction in which the record holder has its principal place of business.
- **Business contacts test**
  - *Executive Officer and Director citizenship/residency test* – Four separate evaluations are required:
    - (1) Citizenship status of executive officers, (2) residency status of executive officers, (3) citizenship status of directors, and (4) residence status of directors. Exchange Act Rules CDI 110.04, Securities Act Rules CDI 203.19
    - Consider what level of inquiry is sufficient and how to memorialize the facts that support citizenship and residency determinations
  - *Asset test* – The company may use the geographic segment information determined in the preparation of its financial statements, or any other reasonable methodology in assessing the location and amount of its assets
  - *Administration of business in U.S. test* – No single factor is determinative. The company must assess on a consolidated basis the location from which its officers, partners, or managers primarily direct, control and coordinate the company’s activities.

Loss of Foreign Private Issuer Status

- Once a company determines at the end of its second fiscal quarter that it no longer qualifies as an FPI, it retains its FPI status until the first day of the following fiscal year.
- Events that may result in immediate loss of FPI status include:
  - Reincorporation into a U.S. jurisdiction; and
  - An initial registration of equity securities under Section 12 of the Exchange Act.

Ramifications of Loss of Foreign Private Issuer Status

- Directors and executive officers would become subject to the reporting and short-swing profits recapture provisions of Exchange Act Section 16
  - Form 3 initial beneficial ownership report due date varies depending on the circumstances which caused the company to lose its FPI status, but could be as early as the day on which the company loses FPI status
- Subject to proxy rules, and Regulation FD
- Must comply with stock exchange corporate governance standards for U.S. domestic companies
- Quarterly reporting and current reporting on domestic issuer forms required
- Financial statements must be prepared in accordance with U.S. GAAP
- Financial information goes “stale” sooner
- Due dates for domestic filers apply (loss of later due date for annual report)
- Loss of option to comply with “home country” corporate governance standards

U.S. Securities Regulatory Regime

- Under U.S. federal securities laws, a foreign private issuer is required to register an offering of securities under the Securities Act, or a class of securities under the Exchange Act, or both in certain circumstances.
- Transactions of securities that are going to be offered or sold (including, re-offers and resales) in the U.S. must be registered under the Securities Act, unless an exemption from registration is available.
- Any class of securities that is to be listed on a U.S. national securities exchange (such as the NYSE or Nasdaq) must be registered under Section 12(b) of the Exchange Act.
- Even without a U.S. listing, registration under Exchange Act Section 12(g) is required if on the last day of a company's most recent fiscal year it has more than $10 million in assets, or 2,000 or more shareholders worldwide, unless exempt.
  - Exemption for foreign issuers with fewer than 300 shareholders resident in the United States (Rule 12g3-2(a)).
  - Exemption by meeting the conditions in Rule 12g3-2(b).
- Note that a company may simultaneously be subject to regulation in (a) home country, (b) country where primary trading market is located, and (c) the United States.
- Foreign private issuers are subject to the liability scheme of the federal securities laws, including Sections 5, 11 and 12 of the Securities Act, and antifraud provisions in Section 10(b) of the Exchange Act, and Exchange Act Rule 10b-5.

U.S. Securities Regulatory Regime

- Rule 12g3-2(b) provides an exemption from registration under Exchange Act Section 12(g) for a foreign private issuer that meets certain conditions:
  - The FPI does not currently have an obligation to file reports under Section 13(a) or Section 15(d) which can arise as a result of a public offering of securities, a listing on a national securities exchange, or voluntary registration under the Exchange Act.
  - The FPI maintains a listing on one or two exchanges in a foreign jurisdiction(s) that comprises at least 55% of its worldwide trading volume (i.e., its “primary trading market”).
  - The FPI publishes in English on its website (or through an electronic information delivery system generally available to the public in its primary trading market) material items of information that:
    - It has made public or been required to make public pursuant to the laws of the country of its incorporation, organization or domicile;
    - It has filed or been required to file with the principal stock exchange in its primary trading market and which has been made public by that exchange; or
    - It has distributed or been required to distribute to its security holders.

Circumstances when Registration is Required

- The foreign private issuer wishes to conduct a public offering in the United States.
- The foreign private issuer wishes to have a class of its securities listed on a U.S. stock exchange (either directly or through ADRs or ADSs).
- The foreign private issuer's worldwide assets and worldwide/U.S. shareholder bases exceed certain levels.

U.S. Public Offerings

- The Securities Act requires registration with the SEC of any offering of a security, unless the transaction is exempt from registration, or a safe harbor applies.
- Securities Act and Exchange Act registration forms available only to FPIs:
  - **Securities Act offerings**
    - Form F-1 – Form prescribed for initial public offerings and other registrations by FPIs.
    - Form F-3 – A short form registration statement that provides for incorporation by reference of Exchange Act filings. The form is available to FPIs that have been an SEC reporting company for at least 12 months, and meet certain reporting and public float requirements, have filed at least one annual report on Form 20-F, and have not defaulted on certain payment obligations.
    - Form F-4 – Form prescribed for business combinations and exchange offers.
    - Form F-6 – Form prescribed for American Depositary Receipts.
  - **Exchange Act registration**
    - Form 20-F – Form generally used by FPIs that want to register their securities under Exchange Act section 12(b) and list on a national securities exchange; but may opt to use Form 8-A, if available.
  - These will be subject to SEC review which can take several months for an initial public offering in the United States. Often no review or much shorter review for subsequent offerings.
  - Requires compliance with Sarbanes-Oxley Act requirements on internal controls over financial reporting and disclosure controls and procedures.

Listing Securities on a U.S. Stock Exchange

- Exchange Act registration of an issuer's securities is required in order to list the securities on a U.S. stock exchange.
- FPI alternatives for trading in the U.S. and related requirements:
  - If securities are to be listed on a U.S. securities exchange such as NYSE/Nasdaq:
    - Securities must be registered under the Exchange Act and the company must file periodic reports with the SEC, either on forms available to FPIs, or, voluntarily, on U.S. domestic forms.
    - Company will be subject to Sarbanes-Oxley Act's auditing, disclosure and certification requirements.
  - If securities are exempt from registration under Exchange Act Rule 12g3-2(b) and the company takes advantage of that exemption:
    - Company will not be required to file reports with SEC and not will not be subject to Sarbanes-Oxley Act.
    - ADRs, if any, will be registered on Form F-6.
    - Securities likely will be quoted on the Pink Sheets.
    - If securities are not listed on an exchange, trading volume and liquidity will be limited.

American Depositary Receipts ("ADRs")

- Shares of foreign companies traded in the U.S. are often traded in the form of ADRs
- An ADR is a negotiable certificate that evidences an interest in an underlying security issued by the FPI.
- ADRs are issued by a U.S. depositary; the underlying securities are issued by the FPI and held in a custodian bank.
- One ADR may represent a portion of a foreign share, one share, or a bundle of shares of a foreign private issuer.
- For U.S. investors, ADRs offer the opportunity to invest in foreign companies without the administrative burden of currency conversions and other cross-border issues.
- ADRs are registered on Form F-6; the underlying shares are registered on Form F-1 (if desired)
- ADRs may be "sponsored" or "unsponsored."
  - In a sponsored ADR, the FPI enters into an agreement directly with the U.S. depositary bank to arrange for recordkeeping, forwarding of shareholder communications, payment of dividends, and other services.
  - An unsponsored ADR is set up without the cooperation of the FPI and may be initiated by a broker dealer wishing to establish a U.S. trading market.

Stock Exchange Corporate Governance Considerations

- NYSE and Nasdaq listed companies are subject to numerous corporate governance requirements.
- NYSE and Nasdaq rules permit FPIs to follow home country law or practice for certain corporate governance requirements, such as:
  - Majority independent board of directors.
  - Fully independent board committees (e.g., Compensation, Nominating & Corporate Governance Committees).
  - Shareholder approval for issuances of shares not involving a public offering.
- Beyond the exchange requirements, FPIs should consider investor perception and expectations to ensure that a broad base of institutional investors will consider purchasing their securities.
  - For example, under ISS guidelines, FPIs are generally covered under a combination of policy guidelines:
    - ISS FPI Guidelines may apply to companies incorporated in governance havens (e.g., Cayman Islands, U.S. Virgin Islands, among others), and apply certain minimum independence and disclosure standards in the evaluation of key proxy ballot items; and/or
    - Guidelines for the market that is responsible for, or most relevant to, the item on the ballot.
- Fiduciary duties of board and officers are those of jurisdiction of incorporation.
- NYSE/Nasdaq require disclosure of any significant ways in which corporate governance practices differ from those required of non-FPIs. Companies required to file annual reports on Form 20-F must disclose in Form 20-F, all others may disclose in an annual report filed with SEC or on company website.

Nasdaq Exceptions to Home Country Compliance Accommodations

- Must promptly notify Nasdaq after an executive officer becomes aware of noncompliance with the exchange's corporate governance requirements.
- Audit committee requirement to comply with Exchange Act Rule 10A-3 independence requirement applies.
- Audit committee members must meet the independence criteria in Rule 10A-3, subject to the exemptions in Rule 10A-3 for FPIs in certain circumstances.
- Compliance with Board Diversity Rule and Board Diversity Disclosure (FPIs may elect to disclose using alternate matrix format).
  - Annual public disclosure required of board-level diversity statistics using a standardized template; and
  - Companies must have, or explain why they do not have, at least two diverse directors, which may be met by having two female directors, or one female director and one director from an underrepresented group.
  - Company may elect to disclose in its proxy statement, or Form 10-K or Form 20-F, or on its website.

Nasdaq Exceptions to Home Country Compliance Accommodations (Cont'd)

- Required to provide a written statement from independent home country counsel certifying that the FPI's practices are not prohibited by the home country's law.
- Sarbanes-Oxley control requirements apply equally to FPIs; SEC rules mandatory
  - Disclosure controls and procedures - management evaluation required as of end of fiscal year (as compared to each quarter).
  - Management evaluation of changes in the company's ICFR that occurred during fiscal year (as compared to each quarter).
  - Management certification requirement applies to annual report on Form 20-F, but does not extend to other reports.
  - Section 402 prohibition on loans to directors and officers applies.

Governance Focus Areas for FPIs

For many FPIs, there are a number of governance requirements that may be challenging to meet and require planning and preparation:

- Audit committee requirements
  - All members independent (under SEC and exchange rules) and financially literate
- Board composition / independence issues
- CEO/CFO certifications on disclosure controls and procedures and completeness of filing included with Form 20-F Annual Report
- Limitations on use of non-GAAP financial measures
- Internal controls requirements
  - Internal controls must be audited by the time of the second annual report on Form 20-F unless the company qualifies as (1) an emerging growth company, or (2) non-accelerated filer
- Personal loans to officers and directors prohibited; violation is a criminal offense

Life As a Public Company

- General disclosure regime
  - Separate disclosure system for FPIs: Forms F-1, F-3 & F-4, Form 20-F, Form 6-K, etc.
  - Confidential submission of registration statements. An FPI conducting an initial public offering, registering a class of securities under Exchange Act Section 12(b) with the SEC for the first time, or conducting an offering within one year of an IPO or Exchange Act Section 12(b) registration, may voluntarily submit a draft registration statement for confidential review provided the company confirms at the time of the confidential submission that it will publicly file its registration statement and nonpublic draft submissions within a certain number of days prior to a road show, if any, or effective date of the registration statement.
  - FPI insiders are exempt from Section 16 “short swing” profit liability and reporting rules
- Proxy rules do not apply; conduct of AGM driven by home country requirements and practical considerations
- Regulation FD does not apply, but general selective disclosure considerations remain.
- Regulation G: Non-GAAP Financial Measure restrictions on a company’s public use of non-GAAP financial measures apply to all disclosures by FPIs, whether or not filed with the SEC
- Insider Trading – Same liability regime applies; similar need for policies, procedures and controls applies
- Enhanced internal controls and disclosure controls required
- U.S. Foreign Corrupt Practices Act requirement to make and keep accurate books and records

Ongoing SEC Reporting/Disclosure Requirements

- Form 20-F – serves as:
  - Annual report (counterpart to Form 10-K for U.S. issuers)
  - General Exchange Act registration statement (counterpart to Form 10)
  - Source of integrated disclosure (counterpart to Regulation S-K)
- Required disclosure topics: Description of Business (including industry and regulatory environment and human capital); Risk Factors; Biographies of board/management; Principal Shareholders; Related Party Transactions; Discussion and analysis of financial performance and results of operations by management; audited financial statements
- Must publicly file material contracts to which the FPI is a party
- SOX Certifications
- Schedule 13D/G beneficial ownership reporting requirements apply

FPIs: Generally Less Demanding Disclosure Requirements

- Executive compensation – disclosure on an aggregate basis permitted, and FPIs are not required to provide Compensation Discussion & Analysis disclosure (or file employment agreements). If an FPI discloses more extensive executive compensation information under its home country requirements or voluntarily, the FPI must disclose the same information under Form 20-F.
- Age of financial statements for securities offerings
- Longer filing timeframes; less frequent disclosure
  - Form 20-F annual report due four months after year-end for all FPIs
  - No specific quarterly reporting requirements (exchanges usually require filing of six-month financials; comfort letter considerations for capital raises)
  - Exchanges also generally require prompt announcement of material information that may reasonably be expected to affect the market for the FPIs securities
  - Item 8.A.5 update – financial statements covering at least six months required nine months after year end to use registration statement
- Foreign language documents: summaries allowed in some cases

Additional Disclosures

- Need to include U.S. dollar currency translations
- Description of applicable foreign exchange and export controls
- Discussion of limitations on rights of foreign shareholders
- Description of impact of non-U.S. taxation related to securities
- Disclosure to investors of difficulties for them in enforcing liabilities under U.S. federal securities laws outside the United States
- Certain items have disclosure requirements that are different from comparable requirements for U.S. domestic filers (e.g., related party transactions)

Form 6-K

- FPIs are not required to file quarterly and current reports on Forms 10-Q and 8-K, but are required to file a Form 6-K promptly after certain material events.
- Form 6-K is used to report, when material, whatever information the FPI:
  - Makes or is required to make public pursuant to the laws of its home country;
  - Files or is required to file with a stock exchange on which its securities are traded, and which was made public by that exchange; or
  - Distributes or is required to distribute to its shareholders.
- Form 6-K itself does not mandate disclosure; it mandates an SEC report for material information that is published either voluntarily or because of another requirement.
- Some topics included in Form 6-Ks include:
  - Earnings information
  - M&A activity and other acquisitions or dispositions of assets
  - Changes in control or in management
  - Change in auditors
  - Events relating to the company's securities, such as stock splits, payment defaults
- Unlike Form 8-K, furnished not filed and not automatically incorporated in shelf registration statements

Financial Statements

- FPIs may prepare financial statements in accordance with (1) US GAAP, (2) IFRS as reported by IASB, or (3) home country GAAP reconciled to U.S. GAAP.
- FPIs that rely on home country GAAP are required to provide a reconciliation to U.S. GAAP.
  - Form 20-F, Items 17 and 18, provide two levels of reconciliation to U.S. GAAP. Item 18 requires the same information as Item 17 plus all of the disclosures required by U.S. GAAP and Regulation S-X.
  - Compliance with Item 18, rather than simpler Item 17, is required for all issuer financial statements in all Securities Act registration statements, Exchange Act registration statements on Form 20-F and annual reports on Form 20-F.
  - Item 17 remains available for pro forma financial statements and significant investee financial statements.
- Audit of last three fiscal years required (can initially be last two years for emerging growth company).
- Audit must be in accordance with auditing standards of U.S. PCAOB.

Going Dark – Deregistration for Foreign Private Issuers

- FPIs may have an easier path to deregistration under Rule 12h-6.
- FPIs may deregister a class of equity securities under section 12(g) and terminate reporting obligations by meeting certain conditions, including a quantitative benchmark designed to measure U.S. interest in its equity securities that does not depend on a numerical count of U.S. stockholders of record.
- Form 15F immediately suspends the FPI's reporting obligations under the Exchange Act. If the SEC has not objected 90 days after filing the Form 15F, the suspension will automatically become a termination. Form 15F takes effect 90 days from filing, and terminates the FPI's 12(g) registration and reporting obligations under section 13(a) and section 15(d).

Going Dark – Deregistration for Foreign Private Issuers

- Conditions for deregistration on Form 15F:
  - must have had reporting obligations under Section 13(a) or 15(d) for at least the 12 months preceding the filing of Form 15F;
  - must have filed at least one annual report while it was registered;
  - must not have effected a registered offering in the United States for the 12 months preceding the filing of the Form 15F;
  - must have filed or furnished all reports required for the 12-month period preceding the filing of Form 15F;
  - must have maintained a listing of the class of securities for at least the 12-month period preceding the filing of the Form 15F; **and** satisfy either of the following conditions:
    - the Average Daily Trading Volume test (U.S. ADTV has been no greater than 5 percent of its worldwide trading volume during a 12-month period), ***or***
    - the record holder benchmark test (less than 300 persons worldwide, or less than 300 persons resident in the United States).
  - 12-month waiting period before a company may file Form 15 if in the 12 months preceding the Form 15 filing the company has delisted a class of equity securities from a U.S. exchange and the U.S. average daily trading volume exceeded 5% of the worldwide trading volume, or the company has terminated an ADR facility to minimize U.S. trading volume.

Delisting from a Stock Exchange

- Must file a Form 25 with the SEC.
- Delisting is effective 10 days after filing.
- Withdrawal from registration under Section 12(b) is effective 90 days after filing.
- Public notice and compliance with requirements of stock exchange required.

Multijurisdictional Disclosure System (MJDS) for Canadian FPIs

- MJDS allows eligible Canadian issuers to register transactions under the Securities Act and to register securities and report under the Exchange Act by use of documents prepared largely in accordance with Canadian requirements.
- Periodic reporting requirement may be satisfied by filing Canadian periodic disclosure filings on Form 40-F for annual reports (must be filed the same day they are filed with Canadian securities regulator), and Form 6-K for interim reports (must be furnished promptly after they are made public).
- For any type of MJDS offering, the Canadian issuer must have at least a three-year history of reporting with a Canadian securities regulatory authority. Except in the case of rights offerings and offerings of certain non-convertible investment grade securities, an issuer also must satisfy specified size tests of minimum market value and/or public float.
- To be eligible to use MJDS registration statements, an issuer must:
  - Be incorporated or organized under Canadian laws;
  - Be an FPI;
  - Generally have a public float (an aggregate market value held by non-affiliates) of at least (CN) $75 million;
  - Not be a registered “investment company.”

Multijurisdictional Disclosure System (MJDS) for Canadian FPIs (Cont'd)

- Benefits of using the MJDS include (i) streamlined registration statement using a prospectus prepared and reviewed in Canada that is primarily, but not exclusively, in accordance with Canadian disclosure requirements, and (ii) compliance with U.S. reporting obligations by filing Canadian disclosure documents.
- Canadian FPIs may effect public offerings in the United States using Forms F-7, F-8, F-10 and F-80.
- Canadian FPIs may elect to use non-MJDS forms to register in the United States using the foreign forms (F-1, F-3, and F-4) or the U.S. domestic forms (S-1, S-3, and S-4), but would be required to provide the more comprehensive disclosure required by those forms, and would be subject to SEC staff review. MJDS registration statements are generally are not reviewed by the SEC staff.

Regulation S

- Regulation S provides an exemption from the Securities Act registration requirements for certain offshore transactions by both U.S. and foreign issuers.
- It is intended to facilitate U.S. companies selling securities solely to persons not in the United States, and U.S. investors buying securities of foreign issuers in overseas markets.
- It is available only for offers and sales of securities outside the U.S. that are made in good faith and not as a means of circumventing the Securities Act registration requirements.
- It is a non-exclusive safe harbor, meaning that an issuer also may rely on another applicable exemption from registration.
- Regulation S offerings are not integrated with other securities offerings for purposes of Rule 152.

Regulation S

- Rule 903 of Regulation S prescribes three categories of transactions that are considered exempt based on the type of securities being offered and sold, whether the issuer is domestic or foreign, whether the issuer is a reporting issuer under the Exchange Act and whether there is a "substantial U.S. market interest" (SUSMI)
- Category 1
  - Offer and sale are made in an "offshore transaction"
  - There are no directed selling efforts in the United States
  - The securities are one of the following:
    - Securities issued by a foreign issuer in which there is no SUSMI;
    - Securities offered and sold in an overseas directed offering;
    - Securities guaranteed by a foreign government; or
    - Securities offered and sold to employees of the issuer or its affiliates pursuant to an employee benefit plan established and administered in accordance with the law of another country.

Regulation S

- Category 2
  - Covers offerings of equity securities of reporting foreign issuers, and offerings of debt securities of reporting issuers (domestic or foreign) and non-reporting foreign issuers that do not qualify for the Category 1 exemption that satisfy these conditions:
    - Offers and sales are made in an “offshore transaction”
    - No directed selling efforts in the United States
    - “Offering restrictions” are implemented
    - There is a 40-day holding period after closing in which no offers or sales of the securities may be made to “U.S. persons”
  - Offering Restrictions: each distributor of the securities agrees (in writing):
    - All offers and sales during holding periods must be in compliance with Reg S or another exemption
    - A commitment not to hedge the securities
    - To place a legend stating the securities have not been registered under the Securities Act on all offering documents and advertising materials

Regulation S

- Category 3
  - Catch-all provision with the most restrictive conditions. Includes offerings of all securities not eligible for Category 1 or 2 that satisfy these conditions:
    - Offers and sales are made in an offshore transaction
    - No directed selling efforts in the United States
    - "Offering restrictions" are implemented
    - For debt securities: 40-day holding period after closing in which no offers or sales of the securities may be made to U.S. persons; securities are held in a global certificate until expiration of holding period and holders certify they are not U.S. persons
    - For equity securities: 1-year holding period after closing in which no offers or sales of the securities may be made to U.S. persons (or six-month holding period if the issuer is a reporting issuer)
  - Offering Restrictions: each distributor of the securities agrees (in writing):
    - All offers and sales during holding periods must be in compliance with Reg S or another exemption
    - Not to hedge the securities
    - To place a legend stating the securities have not been registered on all offering documents and advertising materials

Regulation S

- What is an **offshore transaction**?:
  - Offers are not made to U.S. persons
  - This phrase includes more than just “U.S. persons” (e.g., it includes transient foreigners receiving a telephone sales call in the US)
  - Either the buyer is outside the U.S. (or seller reasonably believes so) or the trade is executed through an offshore securities market
- What are **directed selling efforts**?:
  - Any activity undertaken for the purpose of, or that could be reasonably expected to result in, conditioning the U.S. market for the relevant securities
  - Examples include advertising the offering in publications with a general circulation in the U.S.; mailing printed materials to U.S. investors; conducting promotional seminars in the U.S.; and making offers directed at identifiable groups of U.S. citizens in a foreign country, such as members of the U.S. military
  - Certain communications and advertisements are excluded from the definition including, for example, advertisements required to be published by U.S. or foreign laws, or by regulatory or self-regulatory authorities, such as a stock exchange

Regulation S

- What is “substantial U.S. market interest”?
- For Equity securities:
  - the United States markets were the largest market for that security in the previous year
  - U.S. markets accounted for 20% or more of all trading in that security during the previous year, and less than 55 percent of such trading took place in, on or through the facilities of securities markets of a single foreign country
- For Debt securities:
  - held by at least 300 U.S. persons
  - at least $1 billion of that security is held by U.S. persons
  - at least 20% of the aggregate outstanding principal amount of that security is held by U.S. persons

Resales under Regulation S

- Regulation S also provides a non-exclusive safe harbor for certain resales
- Specifically, Rule 904 sets forth the conditions for offshore resales
  - Only available for securities of FPIs
- Rule 905 imposes certain limitations on resales
- Because Regulation S is a non-exclusive safe harbor, a person may still rely on other safe harbors for resales such as Rule 144

Rule 144A Offerings

- Rule 144A provides a safe harbor for certain resales of restricted securities by any person other than the issuer.
- To qualify for the Rule 144A safe harbor:
  - The securities at issue must be offered and sold only to Qualified Institutional Buyers ("QIBs"), or institutions the seller (or person acting on behalf of the seller) reasonably believes to be QIBs.
  - The seller must take reasonable steps to ensure that the purchaser is aware the seller may rely on the Rule 144A safe harbor provision.
  - The securities offered or sold must not, when issued, be of the same class as a class listed on a U.S. securities exchange.
    - Securities that are convertible or exchangeable into securities that are listed on a U.S. securities exchange and that have an "effective conversion premium" of less than 10%, are deemed under Rule 144A to be of the same class as the underlying securities.
- Purchasers are entitled to obtain from the issuer, upon request, reasonably current information about the issuer.
  - This does not apply to securities of issuers that have Exchange Act reporting obligations, or foreign governments.
- "Rule 144A for life"; no registration requirements

Cross-Border Tender Offer Rules

- Potential acquirers of FPIs can rely on exemptions from SEC rules for certain tender and exchange offers and business combinations.
  - 2 tiers of exemptions:
    - Tier I (10% or fewer U.S. holders): exemption from most U.S. tender offer rules
    - Tier II (40% or fewer U.S. holders): exemption from certain (mainly procedural) provisions that may be inconsistent with non-U.S. rules or practices; no exemption from most filing, dissemination and procedural requirements of the U.S. rules
- Business Combinations
  - Rule 802 — exemption from registration of securities issued in cross-border exchange offers or business combinations (e.g., mergers) to holders of securities in FPIs with limited U.S. ownership:
    - 10% or less of target securities are owned by U.S. resident holders
    - Inquiry of banks, brokers dealers, etc. in relevant jurisdictions required to confirm %
- U.S. holders must receive same documentation (in English) as non-U.S. holders.

Thank You