LATHAM & WATKINS

Number 588 11 April 2007

Client Alert

Latham & Watkins
Corporate Department

The SEC Facilitates Foreign Private Issuer Deregistration Under the Exchange Act

On March 20, 2007, the Securities and Exchange Commission (the "Commission" or "SEC") adopted Rule 12h-6 and amendments to the rules that govern when a foreign private issuer[1] may terminate registration of a class of equity securities under Section 12(g) of the Securities and Exchange Act of 1934 (the "Exchange Act"), and when a foreign private issuer may cease its reporting obligations regarding a class of either its equity or debt securities under Section 15(d) of the Exchange Act.[2] These rules will make it considerably easier for foreign private issuers to deregister their securities and exit the US Securities and Exchange Act reporting system.

"Rule 12h-6 will come into force on June 4, 2007, enabling foreign private issuers (whose fiscal year end is December 31) that are eligible and wish to deregister and suspend their reporting requirements prior to filing with the SEC their annual report on Form 20-F to do so prior to the June 30 filing deadline"

The new rules represent a further liberalization from the original proposals published in December 2005 (the "2005 Proposals") and the reproposals published in December 2006 (the "2006 Proposals"), both of which were intended to facilitate the ability of foreign private issuers to deregister and cease their reporting obligations under the Exchange Act.[3] Rule 12h-6 and the amendments to the other rules will come into force on June 4, 2007, enabling foreign private issuers (whose fiscal year end is December 31) that are eligible and wish to deregister and suspend their reporting requirements prior to filing with the SEC their annual report on Form 20-F to do so prior to the June 30 filing deadline.[4] This *Client Alert* summarizes the deregistration process under the new rules upon their effectiveness and compares it to the current rules as well as to the 2005 Proposals and the 2006 Proposals.

Deregistering Equity Securities

The new rules set out several conditions which foreign private issuers must meet in order to deregister their equity securities. The key condition involves two alternatives which employ a quantitative benchmark. There are three additional conditions which foreign private issuers must fulfil to deregister.

Alternative 1: The 5 Percent Average Daily Trading Volume Test

Under Rule 12h-6, equity securities of foreign private issuers will be eligible for deregistration if the average daily trading volume (ADTV) of that class of securities during a recent 12-month period[5] in the US has been 5 percent or less of the ADTV of those same securities on a world-wide basis.[6] This change is the most important improvement from the current deregistration rules for foreign private issuers. In stark contrast to deregistration rules now in place and the rules proposed in 2005, this new

standard is not based on the number of US holders of the issuer's class of securities or the size of the issuer.[7] In addition, this new standard is measured against *world wide* trading volume as opposed to an issuer's primary trading market – the standard suggested under the 2006 Proposals. This should make it possible for more foreign private issuers to both deregister and to more easily ascertain whether they qualify for deregistration thereby reducing their regulatory compliance costs.

While the new rules do not specify how ADTV is measured (which is consistent with other provisions in the Exchange Act, such as Regulation M, where the concept of ADTV is used), the new rules do provide welcome guidance in two central areas highlighted by many of the comment letters submitted to the Commission on the 2006 Proposals. First, the new rules specify that the number of shares underlying an issuer's American Depositary Receipts (ADRs) shall be included in calculating ADTV.[8] Second, the Commission has clarified that an issuer may include off-market transactions, including ones completed through an alternative trading system, in its calculation of world wide ADTV.[9] In addition, the new rules provide that trading volume related to equity-linked securities, such as convertible debt securities, options and warrants, should be excluded when calculating ADTV.[10]

There are two limits to using the new rules' ADTV standard to ensure that the issuer seeking to deregister under this new standard does not artificially suppress the US ADTV of a certain class of equity securities in order to qualify for deregistration.[11] First, if, within the previous 12 months, the issuer had terminated an ADR facility in the same class of securities and the US ADTV of that class of securities exceeded 5 pecent of the issuer's world wide ADTV at the time of such delisting, it will not be eligible to terminate its reporting obligation under the ADTV standard.[12] Second, if, within that same previous 12-month period, the issuer had delisted the same class of equity securities from a US-based securities exchange or inter-dealer quotation system and the US ADTV of that class of securities exceeded 5 percent of the issuer's world-wide ADTV at the time of such delisting, the issuer will likewise not be eligible to deregister under the ADTV prong of the new rules for a 12-month period.[13]

One of the chief benefits of the new rules over the currently existing ones regarding equity securities is that issuers satisfying the benchmarks described in the new rules will be able to terminate their reporting obligations under Section 15(d) of the Exchange Act permanently.[14] Under the existing rules, such reporting obligations are suspended but could be reinstated depending on the number of US holders over time.[15] This is one of the primary contributors to foreign private issuers' perception of the US Exchange Act reporting system as one where "you can check-in but you can't check-out."[16]

Alternative 2: The 300 Holder Test

As an alternative to the proposed ADTV benchmark provision, the new rules will permit a foreign private issuer to terminate its reporting obligations under the Exchange Act regarding a class of equity securities if, on any date within 120 days before filing for deregistration, the foreign private issuer has less than 300 record holders on a worldwide basis, or who are US residents, in keeping with the 2006 Proposals.[17] The new rules retain the "look through" counting method contained in the 2005 Proposals and the 2006 Proposals for determining the number of holders of securities.[18]

Under the new counting method, an issuer will only have to look through the accounts of brokers, banks and other nominees located in the United States, the jurisdiction in which the issuer is organized and, if different, the jurisdiction of its primary trading market to make this calculation.[19] In addition, if an issuer aggregates the trading volume in two jurisdictions for purposes of determining its primary trading market, it will have to look through nominee accounts in both jurisdictions for purposes of calculating the number of US holders.[20] In undertaking this

analysis, the issuer will be able to rely on an "independent information services provider."[21] Moreover, an issuer will be able to benefit from a presumption previously adopted in respect of the cross-border rules and the definition of foreign private issuer,[22] that if, after reasonable inquiry, an issuer 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, such issuer may assume that the customers are residents of the jurisdiction in which the nominee has its principal place of business.[23]

The inclusion of this record holder test ensures that foreign private issuers who qualified under a similar standard under the existing rules but do not qualify under the ADTV prong of the new rules can still deregister. In addition, the simplification of the counting method of the new rules over the currently existing rules should lower regulatory costs for foreign private issuers.

Additional Conditions for Deregistering Equity Securities

Regardless of whether it utilizes the ADTV alternative or the 300 holder alternative, a foreign private issuer wishing to deregister a class of equity securities under the new rules will have to meet three additional conditions to terminate its reporting obligations.[24] First, a foreign private issuer seeking to deregister will have to have at least a 12-month Exchange Act reporting history, including having filed at least one Exchange Act annual report, and be current in its reports.[25] This condition is intended to ensure that US-based investors have ample time and information upon which to evaluate a foreign private issuer before that issuer terminates its reporting obligations under the Exchange Act.[26]

Second, the equity securities of a foreign private issuer planning to deregister those securities must not have been sold, subject to limited exceptions, through a registered public offering under the Securities Act of 1933 (the "Securities Act") in the 12 months leading up to the attempted deregistration.[27] In contrast to the 2005 Proposals, securities sold via an exemption to the Securities Act will not be subject to this limitation.[28] Consequently, Rule 144A offerings and issuances of securities under Rule 802, among other exemptions to registering under the Securities Act that occur within the previous year, will not delay or prevent the deregistration of a foreign private issuer under the new rules.[29] This represents a substantial increase in the scope of the deregistration rules in comparison with the 2005 Proposals, as many foreign private issuers tap the liquid qualified institutional buyer market by making exempt offerings into US markets while not making any registered offerings.

Finally, a foreign private issuer wishing to deregister a class of its equity securities will have to have had that class of securities listed on an exchange in the issuer's primary trading market for at least 12 months preceding the deregistration filing in the US[30] This is meant to ensure that there is at least one jurisdiction regulating the class of securities that might still be owned by US-based investors.[31] "Primary trading market" under Rule 12h-6 is defined as the market where at least 55 percent of the trading in the class of securities to be deregistered must have taken place through the facilities of a securities market during a recent 12-month period.[32] Although two foreign jurisdictions can be aggregated to calculate this percentage, if this is done, the trading market for the class of securities in at least one of these jurisdictions must be larger than the US trading market for the same class of securities.[33]

Deregistering Debt Securities

A foreign private issuer will also be able to terminate its reporting requirements under the Exchange Act with regard to a class of debt securities under the new rules if two principle criteria are satisfied.[34] First, the issuer will be required to have submitted all Exchange Act required filings, including at least

one Exchange Act annual report,[35] since the debt securities were registered and came under the Exchange Act reporting system.[36] Second, as with "Alternative 2" discussed above, the foreign private issuer must have less than 300 record holders on a world wide basis or who are residents of the US, in either case, on a date within 120 days before filing for deregistration.[37] The method for counting these record holders is the same as for equity securities under the new rules as described above.[38]

Additional Features of the New Rules

The new rules contain additional changes to the existing rules that foreign private issuers should consider in deregistering their securities under the Exchange Act. Many of theses additional changes are consistent with the Commission's 2005 Proposals and 2006 Proposals.

Implications for Mergers and Acquisitions

The new rules provide that a foreign private issuer that succeeds to the reporting obligations of another company following a merger, consolidation, exchange of securities, acquisition of assets or similar transaction can take into account the reporting history of the predecessor company in determining whether it is eligible to deregister under Rule 12h-6.[39] The new rules, in keeping with the 2006 Proposals, attempt to address the concern that the 2005 Proposals would have prevented an issuer that has succeeded to the Exchange Act reporting obligations of an acquired company pursuant to Rule 12g-3 or 15d-5 under the Exchange Act from terminating its reporting obligations even though the issuer satisfies the rule's other requirements.[40]

Under the new rules, 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.[41] 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.[42] 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 during the relevant period.[43] If a registered offering is involved in the business combination, then the resulting entity will have to fulfil all of Rule 12h-6's requirements, most importantly the limitation on not having sold any securities in the US in a registered offering during the previous twelve months.[44] Of substantial practical importance, the new rules – responding to a comment letter from Latham & Watkins LLP respect to the 2006 Proposals – provide that it is not necessary to take into account a predecessor issuer's ADTV when determining whether the ADTV condition is met by a successor issuer to a business combination transaction.[45]

12g3-2(b) Exemption

Under the new rules, foreign private issuers that deregister will be immediately eligible to apply for an exemption under Rule 12g3-2(b).[46] Under the existing rules, eligible issuers have to wait at least 18 months before being sure that they have avoided any obligations to re-register prior to claiming the exemption from registration provided by Rule 12g3-2(b).[47] The new rules will permit a foreign private issuer to claim the Rule 12g3-2(b) exemption: (1) immediately upon termination of its Exchange Act reporting using Rule 12h-6;[48] and (2) upon the condition that the issuer publish in English its home country material required by Rule 12g3-2(b) on its Web site or through an electronic information delivery system that is generally available to the public in the issuer's primary trading market.[49 & 50]

Deregistration Process

Form 15F Disclosure
Under the new rules, a foreign private issuer must file a Form 15F to commence the deregistration process for a class of securities.[51] Through executing and filing Form 15F, the issuer will be certifying[52] that: (1) it meets all of the conditions for terminating its Exchange Act reporting obligations specified in Rule 12h-6;[53] and (2) there are no classes of securities other than those that are the subject of its Form 15F filing for which the issuer has Exchange Act reporting obligations.[54] Form 15F will also require the issuer to provide information that it relied upon in reaching the decision to cease its Exchange Act reporting obligations.[55] This may include disclosure of its reporting history, its last sale of registered securities and, whichever applies, the primary trading market, trading volume data or number of record holders of the subject class of securities.[56]

Post-Filing Waiting Period
As with Form 15 filings under the current rules, the filing of a Form 15F under the new rules will immediately suspend a foreign private issuer's Exchange Act reporting obligations.[57] The Commission will then have 90 days to register any objections to the filing.[58] If the Commission does not object, the class of securities will automatically become deregistered and the corresponding Exchange Act reporting obligations will be terminated.[59] If, however, the Commission rejects the Form 15F or the foreign private issuer withdraws it for any reason, the issuer will then have a 60-day window within which it must re-commence its Exchange Act reporting obligations and submit all missed reports.[60] Crucially, after filing its Form 15F, a foreign private issuer will have no continuing duty to conduct further inquiries to establish its eligibility to remain deregistered.[61] However, an issuer who has filed Form 15F must withdraw its filing if it becomes aware that any of its material submissions no longer hold true as at the date of the original Form 15F filing.[62]

Public Notice Period
In order to alert US investors that have purchased the foreign private issuer's securities about the issuer's intended withdrawal from the Exchange Act reporting system, the new rules will: (1) require an issuer of equity or debt securities (or a successor issuer) 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 Section 13(a) or 15(d) reporting obligations;[63] (2) require such notice to be published through means reasonably designed to provide broad dissemination of the information to the public in the US;[64] and (3) require the issuer to submit a copy of the notice, either under cover of a Form 6-K before or at the time of filing of the Form 15F, or as an exhibit to Form 15F, to the Commission.[65] The originally proposed minimum notice period requirement has been eliminated.[66] Under the new rules, the notice must be published before or on the date of the filing of the Form 15F.[67]

Application to Previous Form 15 Filers

The new rules will permit foreign private issuers that have already terminated the registration of a class of securities under Section 12(g) of the Exchange Act or suspended their reporting obligations under Section 15(d) of the Exchange Act in respect of equity or debt securities by filing a Form 15 under the currently existing rules to terminate permanently their Exchange Act reporting obligations.[68] A foreign company registered under Section 12(g) would benefit by filing a Form 15F under Rule 12h-6 as it will be able to claim the 12g3-2(b) exception immediately upon effectiveness of its Rule 12h-6 termination, as opposed to being subject to an eighteen month waiting period following the filing of a Form 15 pursuant to Rule 12g-4.[69] In addition, a company that previously reported under Section 15(d) of the Exchange Act but suspended its reporting obligations by filing a Form 15 pursuant to Rule 12h-3 could terminate,

rather than merely suspend, its reporting obligations by filing a Form 15F.[70]

A prior Form 15 filer will have to meet three conditions to accomplish this with respect to a class of equity securities: (1) it must file Form 15F;[71] (2) it must meet either alternative quantitative benchmark with respect to such equity securities;[72] and (3) it will have to meet the foreign listing condition described above.[73]

A prior Form 15 filer will have to meet two conditions in respect of its debt securities: (1) it must file a Form 15F;[74] and (2) it must satisfy the new rules' record holder quantitative benchmark.[75]

Unlike other foreign private issuers, prior Form 15 filers will not have to satisfy prior reporting or dormancy requirements to deregister under the new rules.[76] The public notice requirement will also not apply to prior Form 15 filers.[77]

Endnotes

[1] "Foreign private issuer" is defined in Exchange Act Rule 3b-4.

[2] *See* SEC Release No. 34-55540.

[3] *See* SEC Release No. 34-53020 for the 2005 Proposals and SEC Release No. 34-55005 for the 2006 Proposals.

[4] SEC Release No. 34-55540, p. 2. *See also* the SEC's Web site, available at http://www.sec.gov/rules/final.shtml (last visited April 3, 2007).

[5] A "recent 12-month period" is defined in the new rule as meaning a "12-calendar-month period that ended no more than 60 days before the filing date" of the Form 15F seeking to deregister. Rule 12h-6(f)(6).

[6] Rule 12h-6(a)(4)(i).

[7] *See* SEC Release No. 34-55005, pp. 8-9. Thus, the status of the issuer as a "well known seasoned issuer" or "WKSI" will have no bearing on whether the issuer qualifies for deregistration under the new rules. This marks a substantial departure from the 2 005 Proposals. *See* SEC Release No. 34-55005, p. 30.

[8] Rule 12h-6 (Note to Paragraph (a)(4)).

[9] SEC Release No. 34-55540, p. 25. Whereas the calculation of US ADTV must include all transactions, whether on-exchange or off-exchange, Form 15F provides that an issuer may include these off-market transactions in calculating world-wide ADTV as long as it has obtained the trading volume data regarding the transactions from publicly available sources, market data vendors or other commercial information providers, provided that this data does not duplicate already counted trades. SEC Release No. 34-55540, p. 25. Issuers will have to disclose their trading volume data sources as part of the deregistration disclosure process. *See* Item 4.F of Form 15F.

[10] SEC Release No. 34-55540, pp. 27-28.

[11] *See* SEC Release No. 34-55540, pp. 28-32. See also SEC Release No. 34-55005, pp. 30-33.

[12] Rule 12h-6(b)(2).

[13] Rule 12h-6(b)(1). The Commission also provided for transitional rules that grandfather issuers that terminated an ADR facility or delisted equity securities prior to March 21, 2007, thereby enabling such issuers to file a Form 15F in reliance on Rule 12-6's trading volume provision even if, at the time of termination or delisting, its US ADTV exceeded the 5 percent threshold. *See* SEC Release No. 34-55540, pp. 32-33.

[14] Rule 12h-6(a). Note that the same holds true for debt securities. Rule 12h-6(c).

[15] Exchange Act Rule 12h-3(e) (17 CFR 240.12h-3(e)).

[16] *See*, *for example*, Michael R. Bloomberg and Charles E. Schumer, "*Sustaining New York's and the US' Global Financial Services Leadership*," 2007.

[17] Rule 12h-6(a)(4)(ii).

[18] Rule 12h-6(e)(1)(i).

[19] *Id.*

[20] Rule 12h-6(e)(1)(ii). While this represents a significant improvement from the existing rules where an issuer must "look through" the accounts of its holders on a world wide basis, it still involves significant time, effort and expense for an issuer to "look-through" the US and primary trading market jurisdictions.

[21] Rule 12h-6(e)(4).

[22] *See* SEC Release No. 34-55540, p. 48.

[23] Rule 12h-6(e)(2).

[24] *See* Rule 12h-6(a)(1-3).

[25] Rule 12h-6(a)(1). This does not mean that a foreign private issuer must have timely filed all reports required during the twelve month period: "In the event that an issuer determines that it should have filed a Form 6-K during this period, it can do so before it files its Form 15F." *See* SEC Release No. 34-55540, p. 37.

[26] SEC Release No. 34-55540, pp. 35-38.

[27] Rule 12h-6(a)(2). Such exceptions include securities issued (i) to the issuer's employees, (ii) by selling security holders in non-underwritten offerings, (iii) upon the exercise of outstanding rights granted by the issuer if the rights are granted pro rata to all existing security holders of the class of the issuer's securities to which the rights attach, (iv) pursuant to a dividend or interest reinvestment plan and (v) upon the conversion of outstanding convertible securities or upon the exercise of outstanding transferable warrants issued by the issuer; provided that the exceptions in (iii)-(v) are not available in respect of securities issued pursuant to a standby underwritten offering or other similar arrangement in the United States. Rule 12h-6(a)(2).

[28] *See* Rule 12h-6(a)(2) and SEC Release No. 34-55540, p. 38-41.

[29] *See* SEC Release No. 34-55540, pp. 39-40.

[30] Rule 12h-6(a)(3).

[31] SEC Release No. 34-55540, pp. 42-45. This represents a concrete example of comity between regulators in that the proposing release does not distinguish among or between the foreign jurisdictions that will continue to regulate the securities after deregistration from the US.

[32] Rule 12h-6(f)(5)(i).

[33] Rule 12h-6(f)(5)(ii).

[34] Rule 12h-6(c).

[35] Rule 12h-6(c)(1).

[36] *Id.*

[37] Rule 12h-6(c)(2).

[38] *See* Rule 12h-6(e).

[39] Rule 12h-6(d)(1).

[40] *See* SEC Release No. 34-55540, pp. 50-53. *See also* SEC Release No. 34-55005, pp. 59-61.

[41] Rule 12h-6(d)(1)(i).

[42] Rule 12h-6(d)(1)(ii).

[43] Rule 12h-6(c)(2).

[44] *See* SEC Release No. 34-55540, pp. 50-53.

[45] *See* SEC Release No. 34-55540, pp. 52.

[46] Rule 12g3-2(e)(1). *See* Form 15F, Rule 12g3-2(b) Exemption. *See also* SEC Release No. 34-55540, pp. 59.

[47] Exchange Act Rule 12g3-2.

[48] SEC Release No. 34-55540, pp. 59.

[49] Rule 12g3-2(e)(2).

[50] Further, a non-reporting company that has received or will receive a Rule 12g3-2(b) exemption upon application to the Commission, and not pursuant to Rule 12h-6, may publish in English its required home country documents on its Internet Web site or through an electronic information delivery system in its primary trading market rather than submitting the materials in paper to the Commission, as is currently required. Rule 12g3-2(e)(3).

[51] Rule 12h-6(a).

[52] An issuer filing Form 15F must provide the signature required by Form 15F in accordance with Regulation S-T Rule 302. Sec. D, Form 15F (referenced in §249.324) in SEC Release No. 34-55540. Note that the certification required for deregistration is not the same as that required by Rule 13a-14(a) or Rule 15d-14(a) in that certification under the new rules is made by the issuer as opposed to being made by officers of the issuer in their official capacities, thereby entailing personal liability in the case of certifications under Rule 13a-14(a) or Rule 15d-14(a). Rather, as Form 15F stipulates: "[the issuer filing Form 15F] certifies that, as represented on this Form, it has complied with all of the conditions set forth in Rule 12h-6 for terminating its registration under section 12(g) of the Exchange Act, or its duty to file reports under section 13(a) or section 15(d) of the Exchange Act, or both." Instructions to Item 11 – Signature, Form 15F (referenced in §249.324) in SEC Release No. 34-55540.

[53] *Id.*

[54] *See* Form 15F (referenced in §249.324) in SEC Release No. 34-55540.

[55] *Id.*

[56] *Id.*

[57] Rule 12h-6(g)(1).

[58] *Id.*

[59] *Id.*

[60] Rule 12h-6(g)(2).

[61] *See* SEC Release No. 34-55540, p. 58. "After filing Form 15F, an issuer will have no continuing obligation to make inquiries or perform other work concerning the information contained in the Form 15F, including its assessment of trading volume or ownership of its securities." *Id.*

[62] *Id.*

[63] Rule 12h-6(h).

[64] *Id.*

[65] *Id.*

[66] *Id.*

[67] *Id.*

[68] Rule 12h-6(i)(1).

[69] *See* SEC Release No. 34-55540, p. 53.

[70] *Id.*

[71] Rule 12h-6(i)(1).

[72] Rule 12h-6(i)(2)(i).

[73] *Id.*

[74] Rule 12h-6(i)(1).

[75] Rule 12h-6(i)(2)(ii).

[76] *See* Rule 12h-6(i)(3).

[77] *See* Rule 12h-6(i)(3).
