

Client Alert

SEC Proposes Rules to Ease the Deregistration Process for Foreign Private Issuers

On December 23, 2005, the SEC proposed rules to be embodied in a new Securities Exchange Act of 1934 rule, Rule 12h-6. Rule 12h-6 will make major changes to the current deregistration rules that make termination of the Exchange Act registration and reporting obligations difficult for foreign private issuers (even if an issuer has little investor interest in the U.S.) and that permit only suspension of reporting obligations, as opposed to termination of those obligations, for some foreign private issuers.¹ The SEC's proposal is in response to criticisms that the current system predates the internationalization of the securities markets.

Current Deregistration Rules

Under the current Exchange Act registration and reporting rules, a foreign private issuer may be subject to reporting obligations under more than one rule, and terminating obligations under one rule may still leave the issuer subject to reporting obligations under one or more other rules. Currently, a foreign private issuer may only deregister a class of its securities if the class is held by less than 300 U.S. residents or 500 U.S. residents for issuers with less than \$10 million in assets, as of the end of its last completed fiscal year. To determine if a foreign private issuer satisfies one of these standards, the issuer is required to "look through" the record ownership of brokers, dealers, banks or nominees on a worldwide basis and count the number of separate accounts of customers residing in the U.S. for which the securities are held. If the relevant U.S. resident holder threshold is satisfied, the issuer may deregister the securities under the Exchange Act. The issuer may also terminate its reporting obligations under the Exchange Act if the securities had not been registered under the Securities Act of 1933. In contrast, if an issuer has registered the securities under the Securities Act, the issuer may deregister the securities under the Exchange Act but may only suspend, not terminate, its Exchange Act reporting obligations and must resume its reporting obligations any time the threshold is exceeded as of the end of each fiscal year. Thus, as a practical matter, this means that an issuer must determine on a year-by-year basis whether it meets the exemption threshold.

Proposed Deregistration Process Rules

Under proposed Exchange Act Rule 12h-6, a foreign private issuer may permanently terminate, not just suspend, its reporting obligations under the Exchange Act, even if it had registered those securities under the Securities Act, as long as the issuer meets specified criteria. Proposed Rule 12h-6 contains separate provisions for the termination of reporting obligations with respect to equity securities and debt securities, as set forth below.

¹ See SEC Release No. 34-53020; International Series Release No. 1295; File No. S7-12-05. A copy of the Release is available on the SEC's website at www.sec.gov/rules/proposed/34-53020.pdf. See also SEC Press Release No. 2005-176. A copy of the Press Release is available on the SEC's website at www.sec.gov/news/press/2005-176.htm.

Equity Securities Registrants

Proposed Rule 12h-6 allows a foreign private issuer to terminate its Exchange Act reporting obligations for a class of securities if it meets the three conditions below:

- ***The Two-Year Exchange Act Reporting Condition:*** The issuer has been an Exchange Act reporting company for the past two years, has filed or furnished all reports required for the past two years and filed at least two annual reports under Section 13(a);
- ***The One-Year Dormancy Condition:*** The issuer's securities have not been sold in the U.S. in either a registered or unregistered offering during the past 12 months, other than securities:
 - sold to the issuer's employees,
 - sold by selling security holders in non-underwritten offerings,
 - exempt from registration under Section 3 of the Securities Act (except Section 3(a)(10)), or
 - constituting obligations having a maturity of less than 9 months at the time of issuance and offered and sold in transactions exempted from registration under Section 4(2) of the Securities Act (i.e., so called "4(2) commercial paper"); and
- ***The Home Country Listing Condition:*** The issuer has maintained a listing for the preceding two years of the subject class of securities on an exchange in its home country² which constitutes the primary trading market for the securities.

An eligible foreign private issuer must also satisfy one of the following benchmarks:

- ***Public Float and Trading Volume Benchmark:***
 - If the issuer is a well-known seasoned issuer as defined under Rule 405 of the Securities Act ("WKSI"), then the issuer may terminate its obligations as long as it can meet one of the benchmarks below:
 - ***Trading Volume Benchmark:*** (1) The U.S. average daily trading volume of the subject class of securities has been no greater than 5% of the average daily trading volume of that class of securities in its primary trading market during a recent 12 month period, and (2) the U.S. residents held no more than 10% of the issuer's worldwide public float³ at a date within 60 days before the end of that same period; or
 - ***Public Float Benchmark:*** U.S. residents held no more than 5% of the worldwide public float of the issuer's equity securities held by non-affiliates for which there is a reporting obligation at a date within 120 days before the filing date of the Form 15F (described below), regardless of U.S. trading volume.

² "Home country" means the jurisdiction in which the issuer is legally organized, incorporated or established and, if different, the jurisdiction where it has its principal listing.

³ "Public float" means the outstanding voting and non-voting equity securities held by an issuer's non-affiliates. As proposed, when calculating the percentage of its worldwide public float held by U.S. residents, an issuer would include in its worldwide public float only the class(es) of equity securities regarding which there is a current Exchange Act reporting obligation.

- However, if the issuer is not a WKSI, it may only terminate its obligations if it can meet the above Public Float benchmark.
- **Alternate Record Holder Counting Benchmark:** If an issuer cannot meet the Public Float or Trading Volume Benchmark, regardless of whether it is a WKSI or not, it can still terminate its Exchange Act obligations under proposed Rule 12h-6 as long as:
 - the class of securities is held of record by less than 300 persons on a worldwide basis or less than 300 U.S. residents at a date within 120 days before the filing date of the Form 15F; and
 - it satisfies the three conditions set forth above.

It should be noted that, under the proposal, any foreign private issuer that terminates its Exchange Act obligations under proposed Rule 12h-6 would automatically qualify for the Rule 12g3-2(b) exemption which permits an issuer to avoid registration under Section 12(g) of the Exchange Act. If a foreign private issuer wishes to maintain this exemption, it is required to provide material home country documents in English under Rule 12g3-2(b) on its website or through an electronic information delivery system that is generally available to the public in its primary trading market. This exemption would remain effective as long as the issuer complies with the availability of information requirement of the proposed rule, or until either the issuer registers a new class of securities under Section 12 of the Exchange Act or incurs reporting obligations under Section 15(d) of the Exchange Act with respect to securities that were not the subject of the deregistration. Moreover, even if the issuer elects not to maintain the Rule 12g3-2(b) exemption, absent a new registration statement being declared effective, the termination pursuant to proposed Rule 12h-6 of the issuer's reporting obligations under Section 15(d) would be permanent.

Debt Securities Registrants

Proposed Rule 12h-6 has a separate provision dealing specifically with the permanent termination of reporting obligations under Section 15(d) of the Exchange Act with respect to a class of debt securities. Termination of reporting obligations under Section 15(d) for a class of debt securities would be permitted if a foreign private issuer meets these conditions:

- **Section 15(d) Reporting Requirement:** The issuer has filed or furnished all required reports under Section 15(d), including at least one annual report pursuant to Section 13(a) of the Exchange Act; and
- **Record Holder Counting:** At a date within 120 days before the filing date of the Form 15F, the class of debt securities is held of record by less than 300 persons on a worldwide basis or by less than 300 persons resident in the U.S.

Counting Method

In order to facilitate the way a foreign private issuer determines whether U.S. residents hold more than the applicable threshold percentage of its worldwide public float, or whether the number of U.S. residents holding its equity or debt securities meet the applicable threshold, proposed Rule 12h-6 would permit an issuer to:

- limit its inquiry regarding the amount of securities represented by accounts of customers resident in the U.S. to brokers, dealers, banks and other nominees located in the U.S., the foreign private

issuer's jurisdiction of incorporation, legal organization, or establishment and, if different, the jurisdiction of the foreign private issuer's primary trading market; and

- 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 regarding, their shareholders.

The proposed rule would require issuers to count securities as owned by U.S. holders when publicly filed reports of beneficial ownership or information that is otherwise provided to the issuer shows the securities are held by U.S. residents.

New Form 15F

Under current Exchange Act rules, a Form 15 must be filed by a foreign private issuer certifying that it meets the conditions for ceasing its Exchange Act reporting obligations. Under the proposal, a new Form 15F would be required to be filed by a foreign private issuer to provide specific information regarding several items that would enable investors to obtain information regarding the issuer's decision to terminate its Exchange Act reporting obligations. This new form would help the SEC assess whether the issuer qualifies for termination of its Exchange Act reporting obligations. Similar to current rules, the filing of Form 15F would automatically suspend an issuer's reporting duties and, as long as the SEC does not object, the suspension would become permanent 90 days after the filing. The SEC is proposing to revise the rules to allow it, at the request of the issuer, to accelerate the effectiveness of a Form 15F.

Notice Requirement

Under the proposed rule, a foreign private issuer would be required to publish a notice in the U.S. to disclose its intent to terminate its Exchange Act reporting obligations no later than 15 business days prior to filing Form 15F and to submit a copy of the notice under Form 6-K before, or at the time of, filing the Form 15F or as an exhibit to the Form 15F.

Comments Sought

Comments with regard to the SEC proposal are due by February 28, 2006. Information on submitting comments to the SEC can be found on the SEC's website at www.sec.gov/rules/submitcomments.htm.

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January 2006

For Additional Information

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