

***ESCAPING “HOTEL CALIFORNIA”:
SEC PROPOSES NEW RULES FOR DEREGISTRATION FOR NON-US ISSUERS***

“Welcome to the Hotel California / Such a lovely place (Such a lovely place) ... / Last thing I remember, I was / Running for the door / I had to find the passage back / To the place I was before / 'Relax,' said the night man, / 'We are programmed to receive. / You can check-out any time you like, / But you can never leave!”

--- The Eagles, lyrics, “Hotel California” (December 1976).

On December 23, 2005, the United States Securities and Exchange Commission (the “**SEC**”) proposed new rules to make it easier for non-U.S. issuers who have securities registered with the SEC and are therefore required to file periodic reports with the SEC, to deregister such securities and terminate their reporting obligations with the SEC.

Background

A non-U.S. issuer generally becomes subject to U.S. registration requirements if it registers a class of securities in connection with a public securities offering in the U.S. or if it has assets in excess of \$10 million and at least 500 shareholders worldwide or 300 or more U.S. shareholders.

Although non-U.S. companies have traditionally had more limited reporting obligations than domestic public companies, with the advent of Sarbanes-Oxley Act of 2002, the SEC imposed more onerous requirements on domestic and foreign issuers, including the requirement that foreign issuers include a report by management of their internal controls in their Annual Reports to the SEC and for their auditors to attest to, and report on, management’s assessment of the effectiveness of these controls. In light of these additional burdens, a number of non-U.S. issuers and their counsel have been clamoring for an easier “exit” from the SEC’s registration requirements for non-U.S. issuers who no longer wish to have their securities registered in the U.S. and do not seek to continue to maintain a strong public presence in the U.S. capital markets.

Current SEC Rules

Currently, a Non-U.S. issuer may terminate registration of a class of securities and terminate or suspend¹ its reporting obligations with the SEC if the class is not listed

¹ If the issuer has made a public offering of its securities in the U.S. that subjected the issuer’s securities to SEC registration, the issuer may not terminate its reporting obligations under SEC rules. Instead, it may suspend its reporting obligations by meeting certain criteria and making a filing with the SEC, but may be subject to a revived SEC reporting requirement in the future if its number of US shareholders again exceeds the threshold requirements for deregistration.

on a U.S. securities exchange or quoted on Nasdaq and if the class is held of record by fewer than 300 U.S. residents.²

Non-U.S. issuers have found it difficult to deregister from the SEC since:
<ul style="list-style-type: none"> ● even with limited U.S. market interest, the 300 record holder requirement is easily exceeded;
<ul style="list-style-type: none"> ● the time and expense of conducting record ownership inquiries in various jurisdictions makes it difficult and expensive process to determine whether or not an issuer can comply with the 300 record holder requirement; and
<ul style="list-style-type: none"> ● in cases of issuers who are registered with the SEC following an offering of securities in the U.S., those issuers' reporting obligations can only be suspended, rather than terminated; accordingly, such issuers' reporting obligations may be revived at any time.

As a result of current SEC rules, non-U.S. issuers who are registered with the SEC cannot easily exit the SEC's reporting regime. SEC Chairman Christopher Cox has noted that non-U.S. issuers reporting to the SEC are stuck in "Hotel California," a reference to the well-known American pop song cited at the outset of this article and includes the lyrics: "You can checkout any time you like, but you can never leave."³

Proposed SEC Rules

A. Easier Deregistration Requirements for Non-U.S. Equity Issuers. The SEC has proposed Rule 12h-6 to ease the deregistration requirements for non-U.S. equity issuers (the proposed rules do not significantly change the rules for non-U.S. debt issuers). These proposed standards are set forth in the tables below.

Non-U.S. Equity Issuer Requirements

	Requirements	
1.	The Company has been filing reports with the SEC under the Exchange Act of 1934,	

² If the issuer's total assets have not exceeded \$10 million on the last day of each of the issuer's three most recent three fiscal years, the test would be less than 500 U.S. residents. See Exchange Act Rule 12g-4.

³ "The most common concern we hear is that, while it is relatively easy to de-list from a U.S. market, it is exceptionally difficult to terminate the reporting obligation with the SEC. Indeed, in some instances, impossible. The last thing we want our U.S. markets to be known as is that famous place where you can always check in, but you can never leave. As a Californian I can tell you that the reason we get so many visitors and immigrants is that we let them leave if they wish. The Hotel California is a great song, but it is a lousy business model." SEC Chairman Christopher Cox, Speech, "Opening Remarks at Open Meeting," Washington, D.C. (December 14, 2005); available at: <http://www.sec.gov/news/speech/spch121405cc.htm>.

	as amended, for two (2) years.	
2.	The Company has not offered securities in the U.S. for the preceding 12 months, except in limited circumstances.	
3.	The Company has maintained a listing of the same class of securities during the preceding 2 years in its home country.	
4.	One of the following three conditions has been met:	
	a. U.S. residents hold no more than 5% of the issuer's outstanding equity securities held by non-affiliates.	
	b. if the Company is a well-known seasoned issuer, ⁴ (A) the U.S. average daily trading volume of the class of securities is no greater than 5 percent of the average daily trading volume of the same class of securities in the issuer's primary trading market during a recent 12-month period and (B) U.S. residents hold no more than 10% of the issuer's outstanding equity securities held by non-affiliates, or	
	c. the class of securities is held of record by fewer than 300 persons on a worldwide basis or fewer than 300 persons resident in the U.S. (similar to current test under SEC rules, but number of U.S. resident security holders would be determined on a "look-through" basis that is more streamlined than current test).	

Non-U.S. Debt Issuer Requirements

	Requirements	
1.	The Company has been a company filing reports with the SEC under the Exchange Act of 1934, as amended, for one (1) year.	
2.	The class of securities is held of record by fewer than 300 persons on a worldwide basis or fewer than 300 persons resident in the U.S. (similar to current test under SEC rules, but number of U.S. resident	

⁴ A "well known seasoned issuer" is a large issuer with a worldwide market value of its outstanding voting and non-voting equity securities of \$700 million or more. In addition, the SEC has set certain additional threshold criteria in the proposed rule (i.e. the issuer must be timely in its SEC filings and not insolvent).

	security holders would be determined on a “look-through” basis that is more streamlined than current test).	
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B. New Easier Counting Rule. In addition, the SEC’s proposed rule would establish a more practical method of counting U.S. resident security holders. In lieu of conducting a worldwide search as required under the current SEC rules (which can be cumbersome and expensive), a non-U.S. issuer could limit its inquiry into the amount of securities held by U.S. residents to brokers, dealers, banks and other nominees in (a) the U.S., (b) the issuer’s jurisdiction of incorporation, legal organization or establishment, and (c) if different from the issuer’s jurisdiction of incorporation, the jurisdiction of the issuer’s primary trading market.

If after a reasonable inquiry, an issuer is unable to obtain information about the amount of securities represented by investor accounts resident in the U.S., it would be permitted to assume that the investors are residents of the jurisdiction in which the nominee has its principal place of business.

The proposed rule would also provide that a non-U.S. issuer could rely in good faith on information concerning the number of U.S. resident securityholders provided by independent, third-party information vendors, so long as the information vendors ordinarily assist issuers in counting and collecting other information regarding their securityholders.

C. Removal of Gap Period. The new proposed rule would apply an existing exemption under Exchange Act Rule 12g3-2(b) to a non-U.S. issuer immediately upon deregistration of its equity securities. Under the current regime, there is a delay in such application, during which time a non-U.S. issuer may be at risk of being required to re-register with the SEC if the number of its non-U.S. holders increases in the interim period between filing of the application to deregister and the effectiveness of deregistration of its securities with the SEC.

D. Limited Reporting Requirements Upon Post-Deregistration Increase in Shareholders. The SEC has also proposed modifying Rule 12g3-2(b). Rule 12g3-2(b) provides that if a non-U.S. issuer later reaches or surpasses 300 U.S. resident securityholders, the issuer may avoid registration with the SEC if the issuer regularly provides the SEC with copies of public disclosures it makes under its home regulatory regime. The SEC proposes to modify this burdensome requirement by mandating that exempted non-U.S. issuers publish this information electronically, in English, on its website or by using an electronic information system that is available to the public in the issuer’s primary trading market.