

U.S. SECURITIES REGULATION

**LANDER'S GUIDE TO
THE U.S. CAPITAL MARKETS FOR
U.S. AND FOREIGN COMPANIES
AND THEIR ADVISERS**

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JANUARY 2011

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Mr. Lander is the former Chairman of the Committee on Securities Regulation of the New York State Bar Association (“NYSBA”) and the former Chairman of the NYSBA’s Section on Business Law. He also participates in continuing legal education programs and is a frequent chair and speaker at programs sponsored by the NYSBA and New York City Bar, including those on public offerings, private placements and corporate governance.

Preface

This book is a brief, sophisticated look at the U.S. securities laws. The book covers: how to go public; how to do other financial transactions, such as private placements and tender offers; and the ramifications of being a public company. This book is a professional's view of the U.S. laws affecting financial transactions, public companies and capital markets.

The book is intended for businessmen, corporate officers and financial executives and their advisers, investment bankers, accountants and lawyers. The business aspects of corporate finance and running a public company are so intertwined with the laws regulating financial transactions, public companies and the capital markets that an understanding of securities law is necessary to function successfully.

This book is the product of over 25 years experience representing private and public companies and financial institutions based in the United States and abroad. It is intended to educate businessmen and their advisers in a practical way and answer questions clients have asked over the years. The book is also intended to present the regulation of both U.S. and non-U.S. companies equally.

The Introduction and Chapter 1 lay the foundation by discussing the relevant statutes, their application, and the U.S. Securities and Exchange Commission (the "SEC"). Chapters 3, 4 and 5 describe how to conduct a public offering in the United States and the U.S. trading markets. Chapter 6 describes an alternative financing method, the private placement, and Chapter 7 describes how you resell securities to achieve liquidity. Chapter 8 describes the U.S. rules for offering securities outside the United States. These rules are contained in Regulation S under the Securities Act of 1933 (the "Securities Act"). Chapters 9, 10 and 11 describe the ramifications of going public in the United States and listing on a U.S. exchange: (a) ongoing reporting under the Securities Exchange Act of 1934 (the "Exchange Act"); (b) the need to comply with federal corporate governance standards and the corporate governance standards of the relevant U.S. exchange; and (c) officer, director and shareholder reporting. Chapter 12 describes accounting issues important to raising capital and for reporting thereafter to shareholders and the capital markets. Chapter 13 describes tender offers both in the United States and outside the United States. Chapters 14 and 15 describe what happens if you don't play by the rules. The Appendices focus on issues that have been of concern to my clients. Appendix A describes non-legal issues facing management considering going public in the United States. Appendices B and C lay out the quantitative listing requirements for the New York Stock Exchange LLC (the "NYSE"), the NYSE Amex LLC (the "NYSE Amex"), NYSE Arca, Inc. ("NYSE Arca") and the NASDAQ Stock Market LLC ("NASDAQ"). Appendix D describes the requirements that must be met for a security to be quoted on the Over the Counter Bulletin Board ("OTCBB"), which is not an exchange. Last, Appendix E provides a checklist for compliance with the Sarbanes-Oxley Act of 2002 ("SOX").

Guy P. Lander
January 2011

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CHAPTER 1.

INTRODUCTION TO U.S. SECURITIES REGULATION

A. Federal Securities Statutes

Currently, the U.S. Securities and Exchange Commission (“SEC”) administers six statutes:

1. Securities Act of 1933 (“Securities Act”);
2. Securities Exchange Act of 1934 (“Exchange Act”);
3. Trust Indenture Act of 1939 (“Trust Indenture Act”);
4. Investment Advisers Act of 1940 (“Advisers Act”);
5. Investment Company Act of 1940 (“Investment Company Act”); and
6. Securities Investor Protection Act of 1970 (“SIPA”).

The Acts most securities lawyers deal with are the Securities Act and the Exchange Act. Also of general interest are the Trust Indenture Act, the Advisers Act and, to a still lesser extent, the Investment Company Act.

B. The Securities Act and the Exchange Act

This guide generally discusses the Securities Act and the Exchange Act. Generally, the Securities Act covers public offerings, i.e., the distribution of securities offered on a relatively large scale. The Securities Act requires that securities distributed to the public be registered with the SEC and that information be disclosed by disseminating a prospectus to those offered the securities. Generally, the Exchange Act regulates securities and related matters after the securities have been distributed, i.e., when they are in the secondary trading markets. The Exchange Act requires companies with publicly traded or otherwise widely held securities to register those securities with the SEC and provide continuous disclosure concerning the company.

The U.S. securities laws are largely based on disclosure on the theory that full disclosure of the material facts about an issuer and its business will lead to the fair pricing of its securities and the maintenance of fair and efficient capital markets.

C. State Securities Laws

In the United States, federal and state governments have separate, independent securities laws. The state securities laws are called “blue sky” laws. The state securities laws are unaffected by federal securities laws, except where state law is specifically preempted by federal law.

D. The SEC

The SEC is the regulatory agency of the U.S. government responsible for administering and enforcing federal securities laws. The SEC has over the years created a large body of precedent through regulations, interpretive rulings, “no-action letters,” administrative orders and

cases instituted in federal courts. It is a so-called “independent” agency.

E. The Integrated Disclosure System for Foreign Private Issuers

The SEC developed the integrated disclosure system for foreign private issuers to balance the needs of foreign issuers seeking to access the U.S. capital markets with the SEC’s primary mandate, investor protection. Consequently, the foreign integrated disclosure system does make some accommodations for foreign practices and policies. The integrated disclosure system for foreign private issuers is discussed throughout this book.

1. Foreign Private Issuer Defined

The foreign integrated disclosure system (and the Multijurisdictional Disclosure System (“MJDS”), discussed in F. below) is limited to “foreign private issuers.” A “foreign private issuer” is any foreign issuer, other than a foreign government and its political subdivisions, unless it flunks by meeting both of the following tests:

- (a) More than 50% of its outstanding voting securities are owned directly or indirectly by U.S. residents; and
- (b) Any one of the following:
 - (i) more than 50% of its executive officers or directors are citizens or residents of the United States,
 - (ii) more than 50% of its assets are located in the United States, or
 - (iii) its business is principally administered in the United States.

This definition requires the issuer to “look through” the record holder to the beneficial owner where the record holder is a financial intermediary, i.e., a bank, broker-dealer or depository, located in: (a) the United States, (b) the issuer’s home jurisdiction, or (c) the primary trading market for the issuer’s securities. When making this determination, the issuer must also accept information on U.S. ownership that has been provided to the issuer or that appears in public filings.

2. Foreign Private Issuer Eligibility - Form 20-F

Issuers test their eligibility to use the forms and rules available to foreign private issuers once a year, on the last business day of their second fiscal quarter.

3. Canadian MJDS Eligibility - Form 40-F

MJDS issuers test their eligibility as foreign private issuers at the end of their second fiscal quarter and test their eligibility to file annual reports on Form 40-F as of the end of their fiscal year.

4. Change in Status

If a foreign issuer determines that it no longer qualifies as a foreign private issuer on the last business day of its second fiscal quarter, it must comply with the reporting requirements and use the forms for U.S. companies beginning on the first day of the fiscal year following the determination date. This gives issuers six months advance notice that they must transition to the U.S. forms and reporting requirements. In contrast, a reporting company that qualifies as a foreign private issuer would be able to avail itself of the accommodations permitted to foreign private issuers, including use of the foreign private issuer forms and reporting requirements, beginning on the determination date on which it establishes its eligibility as a foreign private issuer. There is no specific requirement that the issuer notify the market of a change in its foreign private issuer status.

5. Benefits for Foreign Private Issuers

Foreign private issuers receive the following accommodations that are not available to U.S. issuers:

(a) The Securities Act

- (i) Confidential submission of registration statement to the SEC for first-time registrants.
- (ii) Ability to use U.S. generally accepted accounting principles (“U.S. GAAP”), International Financial Reporting Standards (“IFRS”) or local GAAP.
- (iii) Ability to resell Regulation S equity securities without Rule 905 (i.e., Regulation D type) resale restrictions.
- (iv) Exemptions from registration for certain cross-border rights offers, exchange offers and business combinations.

(b) The Exchange Act

- (i) Filing of annual reports on Form 20-F rather than on Form 10-K:
 - (A) Later filing deadlines.
 - (B) Less demanding executive compensation disclosure.
 - (C) Home country GAAP reconciled to U.S. GAAP or IFRS.
 - (D) Less extensive disclosure for related parties.

- (E) More lax filing requirements for employment or compensatory plans with management or directors as exhibits.
- (ii) No Form 10-Q quarterly reporting or Form 8-K current reporting obligations; Form 6-K is a “wrapper” or cover page for home country disclosure.
- (iii) No Section 16 shareholder reporting or liability for short-swing profits.
- (iv) No Section 14 proxy and information statement requirements.
- (v) Audit committee independence accommodations for certain foreign private issuers unable to fully comply with the audit committee independence requirement in Rule 10A-3 under the Exchange Act.
- (vi) Deregistration under the Exchange Act is available.
- (vii) Exemptions are available under cross-border tender offer rules.
- (viii) More limited executive compensation disclosure.
- (c) The Exchanges

The rules of the NYSE, NASDAQ and other U.S. securities exchanges permit listed foreign private issuers to claim exemptions from some of their corporate governance requirements, including exemptions from the requirements that the board be composed of a majority of independent directors and that the board have a compensation or nominating committee (or similar committee) meeting certain requirements. However, foreign private issuers availing themselves of these exemptions must disclose on Form 20-F how their corporate governance practices differ from those that would otherwise be required.

F. The MJDS

Also discussed in this book is the U.S. Multijurisdictional Disclosure System (“MJDS”), which makes it much easier for qualified Canadian companies to offer securities, file continuous disclosure information thereafter and register exchange offers and business combinations in the United States. The MJDS enables qualified Canadian issuers to file with the SEC and distribute to U.S. investors disclosure documents prepared and reviewed under Canadian law.

G. Filing Electronically: EDGAR

U.S. and non-U.S. issuers must use the SEC’s Electronic Data Gathering, Analysis and Retrieval (“EDGAR”) system for nearly all SEC filings. Documents such as registration statements for offerings of securities, annual reports and most current reports must be filed electronically. Additionally, all exhibits and attachments to SEC filings must be filed

electronically, except for exhibits and attachments previously filed in paper form, which may generally be incorporated in an EDGAR filing by reference.

There are only limited exceptions to the requirement to file electronically.

Generally, all filings in EDGAR must be made in English. Non-English documents must be fairly and accurately translated into English for filing in accordance with the SEC's rules on foreign-language documents.

H. Interactive Data: XBRL

U.S. and non-U.S. issuers that prepare their financial statements in accordance with U.S. GAAP or IFRS as issued by the International Accounting Standards Board ("IASB IFRS") must provide their financial statements in eXtensible Business Reporting Language ("XBRL"). XBRL is a form of electronic communication that involves interactive electronic tagging of both financial and non-financial data.

The SEC has adopted a three-year phase-in program of XBRL beginning with periodic reports on Forms 10-Q, 20-F or 40-F containing financial statements for a fiscal period ending on or after June 15, 2009.

I. Confidentiality

Foreign private issuers that are registering with the SEC for the first time may submit registration statements for review on a confidential basis. Those registration statements remain confidential until their public filing (which is usually when printing a preliminary prospectus). In almost all other circumstances, issuers must file registration statements and Exchange Act reports publicly. These documents, including any exhibits, such as material contracts, become available shortly after filing (through the SEC's EDGAR database). Additionally, the SEC makes public both its comment letters on issuers' registration statements and required Exchange Act reports, as well as issuers' responses to those comments, within 45 days of the end of the SEC's review process.

The Securities Act and the Exchange Act include rules detailing how confidential treatment may be obtained for information contained in documents that are required to be filed with the SEC. However, the SEC has historically been unwilling to grant broad requests for confidential treatment, particularly of contractual terms.

CHAPTER 2.

WHAT IS A SECURITY?

A. Introduction

The U.S. securities laws apply to transactions in securities. Consequently, whether the securities laws apply depends on whether a “security” is involved.

The term “security” is defined in the Securities and Exchange Acts in broad terms which are intended to include within the definition the many types of instruments commonly thought of as securities within the commercial world.

The Securities Act defines “security” as follows:

Section 2(a). When used in [the Securities Act], unless the context otherwise requires—

- (1) The term “security” means any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

The Exchange Act defines “security” as follows:

Section 3(a). When used in [the Exchange Act], unless the context otherwise requires—

- (10) The term “security” means any note, stock, treasury stock, security future, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, any put, call,

straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or in general, any instrument commonly known as a “security”; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker’s acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.

While there are very slight differences between the two lists, the U.S. Supreme Court has stated that the definitions of security under the two statutes will be treated as virtually identical.

Generally, the Supreme Court has held that each type of financial instrument must be analyzed separately using a different test appropriate for each instrument. If an instrument is clearly within the statutory definitions, like common stock, then the instrument is a security. If an instrument is unusual and not easily characterized as a security within the definitions, then the analysis should look to the economic realities of the transaction, rather than just its form, to determine whether the securities laws apply.

B. Investment Contracts and Unorthodox Securities

The definitions of a security include a category of instruments called “investment contracts,” which is a catch-all term for transactions not specifically included in the definition lists. The courts have created rules, based largely on the words “investment contract,” for determining what elements of a transaction constitute a security in situations not specifically enumerated in the Acts in order to prevent evasion of the protections intended by the Acts.

The touchstone case is a Supreme Court case, *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946), which has been modified by later cases. Generally, under the *Howey* test, an investment contract is defined as a contract, transaction or scheme whereby a person (a) invests money (or other consideration), (b) in a common enterprise, and (c) is led to expect profits, (d) substantially from the efforts of others. In *Howey*, the defendants sold to plaintiffs small plots of land in citrus groves together with a service contract for the cultivation, harvesting and marketing of the fruit. The defendants then gave each investor a percentage of the overall profits. Looking at the underlying economic reality, the Supreme Court examined the investment as a whole and how it was marketed and found the transaction to be an investment contract under the federal securities laws.

C. Other Instruments

1. Stock: Generally, where an instrument is labeled stock and possesses the characteristics of stock, the instrument will be considered a security. This includes sales of

securities as part of the sale of an entire business but excludes sales of shares in cooperative apartments.

2. Notes: Based on the Exchange Act's definition of a security, notes with a term of more than nine months are presumed to be a security but that presumption may be rebutted by showing that the note in question is within a previously recognized judicial exception, or is sufficiently similar to a previously recognized judicial exception or by convincing the court to add a new instrument to the list of judicial exceptions (the "family resemblance test").

3. Partnership, Joint Venture and Limited Liability Company Interests: Partnership, joint venture and limited liability company interests may be securities depending on the circumstances. The test used for determining whether these interests are securities in a particular case is the *Howey* test. Generally, interests in general partnerships and similarly structured limited liability companies are not considered securities because the partners (and members) are involved in the activities of the entity and do not rely on the efforts of others. But interests in limited partnerships and similarly structured limited liability companies are securities because investors rely on the management efforts of others.

CHAPTER 3.

THE REGISTRATION PROCESS FOR PUBLIC OFFERINGS

A. Introduction

1. Why Consider Going Public?

Generally, the single best reason to “go public,” i.e., to conduct an initial public offering (“IPO”), is that the Company has reached a stage in its development where it needs funds to grow. Shareholders may also want to sell part of their interest in the Company and obtain cash for their investment.

2. Advantages and Disadvantages of a Public Offering

(a) Advantages:

- (i) Compared to debt, there is no obligation to repay principal and no interest payments.
- (ii) A trading market is established for the Company’s securities which enables shareholders to realize gains and obtain cash for their investment in the Company.
- (iii) An aftermarket facilitates later financings, i.e., future public offerings and private placements.
- (iv) Securities of a public company can be used to build the Company through acquisitions.
- (v) Securities of a public company can be used to create incentives for employees.
- (vi) A public company is believed by many to be more prestigious than a private company.

(b) Disadvantages:

- (i) Previously confidential information must be disclosed.
- (ii) Ownership is shared with public investors and management must deal fairly with them.
- (iii) Management loses flexibility.
- (iv) Management is usually preoccupied with keeping the Company’s stock price up.

- (v) Company incurs continuing increased costs once it is public.
- (vi) Founders risk a possible loss of control, depending on the circumstances.

3. Once a Company Decides on a Public Offering

Once a company decides on a public offering two issues arise, the underwriting process and the registration process. The Company usually needs a professional to sell its securities - the underwriter. And, by law, the securities must be registered before the underwriter can sell them. Counsel educates and advises Company management throughout the underwriting process, and counsel assists the Company in registering its securities.

B. Registration of Securities

1. Section 5 of the Securities Act: prohibits any offer of a security unless a registration statement has been filed with the SEC as to such security, and prohibits the sale or delivery of a security unless a registration statement is in effect as to such security. Generally, the Securities Act prohibits public distributions of securities without registration and requires the delivery of a prospectus that discloses relevant information to investors.

(a) Registration and Disclosure

Before the underwriter can sell securities, the Company must register the securities. The Securities Act prohibits anyone from selling securities to the public unless a registration statement is in effect covering the securities or an exemption from registration is available. The Securities Act does not evaluate investments, i.e., it does not permit good investments and prohibit bad investments. Rather, the Securities Act forces the disclosure of all relevant information so that each investor can make his own informed decision whether or not to buy the security. The Securities Act is a Truth-In-Securities Statute.

(b) Section 5(c) - The Pre-Filing Period

A public offering in the United States is usually made through an underwriting syndicate led by one or more managing underwriters (also called lead underwriters or the representatives). Accordingly, when a company decides to raise funds through an underwritten public offering, it chooses an investment banking firm to manage the underwriting and negotiates the terms of the offering with that underwriter.

When structuring the offering, some of the terms negotiated by the issuer and managing underwriter are: the type of security to be sold (e.g., common stock); the size of the offering (e.g., the approximate number of shares to be sold); the contemplated price range per share or a formula or mechanism for determining the price; the nature of the offering (e.g., whether the securities will be sold by the issuer only, by stockholders only, or both or whether

the offering will be a rights offering);¹ the underwriters' compensation and expenses; and "lock-up" periods during which stockholders cannot sell their shares into the public markets.

(i) Preliminary Negotiations With the Proposed Underwriter

As discussed below, in a "firm commitment" underwriting, the underwriter buys the securities from the issuer and then resells the securities to the public. Under Section 5(c) of the Securities Act, it is unlawful to "offer to sell or offer to buy . . . [a] security, unless a registration statement has been filed as to such security." However, preliminary negotiations with the proposed underwriter may be conducted. Under Section 2(a)(3) of the Securities Act, an "offer to sell" does "not include preliminary negotiations or agreements between an issuer . . . and any underwriter or among underwriters who are or are to be in privity of contract with an issuer"

(ii) Letter of Intent, Also Called an Engagement Letter

Frequently, but not always, the Company will enter into a letter of intent with the underwriter. Once the Company has selected an underwriter, the Company will negotiate the terms of the offering with the underwriter and sometimes the parties will outline the terms of the offering in a letter of intent. However, even when a letter of intent is used, it is usually not binding.

The letter of intent identifies the nature of the underwriting commitment. There are basically two types of underwriting commitments: firm commitment and best efforts.

(A) Firm Commitment: the stronger of the two and the type usually used by reputable underwriters.

In a firm commitment underwriting, the underwriter buys the securities from the Company at slightly less than the public offering price and then resells the securities to the public at the public offering price. Any securities the underwriter cannot sell, it owns.

The "spread" between the purchase price and the resale price is the underwriter's commission.

¹ If a foreign issuer plans to raise capital through an equity offering, the issuer often may choose or be required under local law to grant rights to its existing shareholders to purchase those shares. In a "rights offering," the issuer offers to sell its securities to existing shareholders for cash through the exercise of subscription or preferential rights granted to those shareholders, usually in proportion to the amount of securities of the class being offered that are held by each of them on the record date for the offering. To encourage shareholders to exercise the rights, the exercise price usually is set at a discount from the market price or, if there is no public market at the time of the rights offering, at a discount from the price at which the underlying securities are expected to trade.

(B) Best Efforts: the weaker of the two.

The underwriter makes no commitment to buy any securities. Rather, it agrees to use its “best efforts” to sell the securities as agent for the Company. If buyers cannot be found, the securities remain unsold.

The letter of intent identifies the conditions that the underwriters expect the Company to meet, e.g., a certain level of earnings. It provides who pays expenses, particularly if the underwriting is completed. Sometimes, the Company pays all the expenses. Sometimes the underwriter will pay its legal and other out-of-pocket expenses or agree to a maximum amount of such expenses to be paid by the Company. The letter of intent is not a binding underwriting commitment. The underwriting agreement contains the actual binding underwriting commitment and it is not signed until just before, or shortly after, the registration statement becomes effective.

(iii) Negotiations With Selling Stockholders

Negotiations with selling stockholders are not explicitly exempt from registration.

(iv) Rule 135 - Notice of a Proposed Registered Offering

Rule 135 under the Securities Act permits an issuer or a selling security holder (and any person acting on behalf of either of them) to make a limited public announcement of a proposed registered offering before the filing of a registration statement. Under Rule 135, a notice of a proposed registered offering is not deemed an “offer” if the notice: (1) states that it does not constitute an offer of any securities for sale, and (2) contains no more than the Rule’s specified information, without naming the underwriters.

2. The Registration Statement

(a) Description

The registration statement is the document used for both registering the securities and disclosing to investors all relevant information necessary to enable them to make an informed investment decision. The disclosure given to investors is in the form of a prospectus included within the registration statement. The registration statement (actually, the prospectus within it) describes the Company’s business, the securities offered and the terms of the offering. The SEC has published numerous forms and rules which specify the information required to be in the registration statement. The registration statement forms used for U.S. issuers, non-U.S. issuers and certain Canadian issuers are discussed in the next chapter.

(b) Contents of the Registration Statement

Generally, the registration statement consists of two parts: Part I - the Prospectus, and Part II - Supplemental Information.

(i) Part One - the Prospectus:

The prospectus comprises most of the registration statement. The prospectus is a booklet that describes the Company, the securities to be offered and the terms of the offering.

Section 10(a) of the Securities Act sets forth the contents required for a full statutory prospectus (i.e., a final prospectus), and Section 10(b) of the Securities Act directs the SEC to adopt rules permitting the use of a prospectus for offers made after the registration statement has been filed that partially omits (or summarizes) the information required in a Section 10(a) prospectus. Furthermore, even under Section 10(a), which deals with the full statutory prospectus, prospectuses may be used which omit such information as the SEC may designate. Consequently, without referring to its Section 10(b) power, the SEC adopted Rule 430 under the Securities Act which permits the use of a preliminary prospectus for offers made after the registration statement is filed but before it is in effect.

In IPOs and other heavily marketed offerings, a preliminary prospectus usually is distributed widely to potential investors after the registration statement has been publicly filed. The preliminary prospectus is generally intended to be complete (i.e., to contain the same information as the final prospectus) except for pricing and other information about the offering not available or not determined when the registration statement is filed. Where the Company was not subject to the reporting requirements of the Exchange Act before filing the registration statement (generally, for a Company's IPO in the United States), Instruction 1 to Item 501(b)(3) of Regulation S-K requires the preliminary prospectus first "circulated" (i.e., distributed to the market) to include: (1) an estimated price range (which the SEC has stated may not be wider than the greater of \$2 or 10% of the high end of the range); and (2) an estimated maximum offering size. However, the SEC has frequently permitted foreign issuers that are listed in their home country before filing to provide share price information for the home market as of a recent date instead of the price range information discussed above. In IPOs, a preliminary prospectus must be delivered to every person who is expected to receive a confirmation of sale at least 48 hours before the confirmation is sent (see G.1. below).

Formerly, a final prospectus (i.e., a prospectus containing all required information) had to be delivered to investors before or when their purchases were consummated (i.e., before or when they received written confirmation of the sale or the security, whichever occurred first). Now, for most registered offerings, this "delivery" requirement will be considered satisfied if: (1) the final prospectus is timely filed with the SEC (i.e., by the time required under Rule 424(b) under the Securities Act);² or (2) the Company has made a good faith and reasonable effort to timely file the final prospectus and files it as soon as practicable after discovery of the failure to file. Accordingly, for most registered offerings, the final prospectus is not given to investors, but it is available for inspection at the SEC's Public Reference Room in Washington, D.C. and on the SEC's web site.

² Usually, the final prospectus must be filed within two business days after pricing.

(ii) Part Two - Supplemental Information:

This part of the registration statement is not given to investors, but it is available for inspection at the SEC's Public Reference Room in Washington, D.C. and on the SEC's web site.

(c) Preparing the Registration Statement and Accounting

For first-time non-U.S. registrants, often an English language annual report or Euromarket offering circular can form a basis from which to start when drafting the registration statement. After the registration statement is drafted by the issuer and its counsel, the initial draft is reviewed by the managing underwriter and its counsel and several drafting sessions are held to work on the disclosure.

A foreign issuer may need a considerable amount of time to prepare its registration statement if it has not previously listed its securities on a U.S. exchange or arranged for their being quoted on the OTC Bulletin Board. Where a foreign issuer has not previously registered under the Securities Act or the Exchange Act, the amount of time needed to complete a draft of the registration statement often depends largely on the amount of time needed to prepare consolidated annual financial statements of the issuer, audited by an independent auditor and accompanied by an audit report. The required annual financial statements (and any required financial statements for interim periods) generally must either: (1) be prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) or International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB); or (2) be reconciled to U.S. GAAP, if prepared using non-IASB IFRS or home country GAAP. The required annual financial statements, which may necessitate substantial restatement and revision of the foreign issuer's usual financial statements, are: (1) audited consolidated statements of income, cash flows and changes in shareholders' equity for the three most recent fiscal years; and (2) audited consolidated balance sheets as of the end of the three most recent fiscal years. However, there are certain exceptions to these requirements. First, a foreign issuer need not provide a balance sheet for the earliest of the three years if that balance sheet is not required by a jurisdiction outside the United States. Second, the SEC provides an accommodation for first-time foreign registrants. Specifically, for a foreign issuer's initial registration statement (whether filed under the Securities Act or the Exchange Act), if the primary financial statements are prepared in accordance with U.S. GAAP, the earliest of the three years of financial statements may be omitted unless the issuer has already included that information in a filing made under the Securities Act or Exchange Act. Third, during an eligible foreign issuer's first year of reporting under IFRS as issued by the IASB, it may file two years (rather than three years) of income statements, cash flow statements, statements of changes in shareholders' equity and balance sheets.

A foreign issuer's registration statement also must include certain income statement and balance sheet items (selected financial data) regarding the issuer, for the five most recent fiscal years, presented in the same currency as the financial statements. However, selected financial data for either or both of the earliest two years of the five-year period may be

omitted if the issuer: (1) represents to the SEC before or when the registration statement is filed that the information cannot be provided, or cannot be provided on a restated basis, without unreasonable effort or expense; and (2) discloses in the registration statement that data for the earliest two years have been omitted and explains the reasons for the omission. Nevertheless, if some of the required data (e.g., revenues) is available for the earliest two years of the five-year period, that data usually should be provided. Required selected financial data may be prepared in accordance with the GAAP used to prepare the foreign issuer's primary financial statements. If the foreign issuer's primary financial statements are prepared in accordance with U.S. GAAP or IFRS as issued by the IASB, the selected financial data need not be reconciled to U.S. GAAP. If the issuer's primary financial statements are prepared using non-IASB IFRS or home country GAAP, the selected financial data must be reconciled to U.S. GAAP, but only for: (1) those periods for which the issuer is required to reconcile the primary annual financial statements, and (2) any interim periods.

To assist foreign issuers with accounting and other procedural issues concerning registration, the staff of the SEC will meet with a foreign issuer that has not previously registered securities with the SEC and its counsel to resolve difficult issues before the registration statement is filed.

(d) Process and Lawyer's Role

A Company registers its securities by preparing a registration statement, filing it with the SEC and the SEC declaring it to be in "effect." One of the lawyer's roles is to assist the Company in registering its securities. The lawyer assists the Company in preparing the registration statement, ushers it through the SEC review process and arranges for it to be declared effective by the SEC. Preparing the registration statement is a cooperative endeavor. The Company's attorneys prepare the registration statement working with management, Company accountants, the underwriter and its counsel.

C. SEC Review of the Registration Statement

1. Review Process

(a) Once prepared, the Company's chief executive officer ("CEO"), chief financial officer ("CFO") and at least a majority of directors sign the registration statement and it is filed with the SEC.

(b) At the filing, the issuer must pay the SEC a registration fee.

(c) Under the SEC's procedures for "selective review," almost all first-time registrants and only a small percentage of repeat registrants are selected for full review. On full review, the SEC assigns two staff members to review the registration statement. They each review the registration statement to see whether it appears to comply with the proper form and appears to provide proper disclosure. One staff member reviews and prepares comments on legal matters and the other reviews and prepares comments on accounting matters. When they complete their review, they send a Letter of Comments to the Company and its attorneys. The Letter of Comments states the ways in which the registration statement appears to be deficient,

and contains any questions the SEC may have about the registration statement and any suggestions it has for improving disclosure.

2. Replying to Comments

The Company's attorneys and accountants either comply in full with the comments or negotiate their reply to difficult comments with the staff. The registration statement is amended and refiled. There may be a second and third round of comments and amendments.

3. Length of Time of SEC Review

Generally, the SEC review may take one or two months. Within a couple of weeks after filing, the staff will inform you of the schedule. For IPOs, the initial SEC review will take at least 30 days. SEC review of the first amendment to the registration statement generally takes two weeks or so, with the review time shortening somewhat for further amendments as the number of comments diminishes. However, these time periods may vary widely depending on many factors including the complexity of the filing and the workload of the staff at a particular time.

4. Going Effective

Once the staff is satisfied with the registration statement, the SEC orders the registration statement to be in effect (technically, by acceleration of effectiveness) under Section 8(a) of the Securities Act.

D. Due Diligence - Making Sure the Registration Statement is Accurate and Complete on the Effective Date

1. Section 11(a) – Liability

(a) Section 11(a) of the Securities Act creates an express right of action for investors when a registration statement contains untrue statements of material fact or misleading omissions of material fact. Section 11(a) is a strict liability provision, subject only to the defenses discussed below.

(b) When the SEC declares a registration statement effective, it has not approved the registration statement; it has merely completed its review of the registration statement to see whether, on the surface, it appears to comply with the proper form and appears to provide the proper disclosure. The SEC does not really know whether the registration statement discloses all it should, or whether the disclosure made is accurate and complete.

2. Those Liable for Misstatements or Omissions

The Company, all signers of the registration statement, all directors, all underwriters, and all accountants, engineers, appraisers and other named experts, may be held liable for misstatements or omissions in the registration statement. Therefore, all must make sure that the registration statement is accurate and complete when effective. The registration

statement must disclose all information that may be material to an investor and may not be misleading.

3. Section 11(b) – A Defense

(a) Section 11(b)(3) of the Securities Act provides a defense to Section 11(a) liability for misstatements or omissions found in a registration statement. Any person other than the Company is absolved of Section 11(a) liability for any part of the registration statement not made under the authority of an expert provided that the defendant “had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading.” The defense is the same for any portion of the registration statement purporting to be made on the authority of an expert (e.g., financial statements) except there is no requirement of a “reasonable investigation” (unless the person asserting the defense is the expert in question).

(b) The “reasonable investigation” referred to in Section 11(b)(3) is called the “due diligence” investigation.

(c) The due diligence investigation verifies each material fact in the registration statement before going effective and serves two functions: (i) to establish the Section 11(b)(3) defense; and (ii) to find potential problem areas and disclose them to protect against future litigation.

E. Publicity

1. Statutory Scheme

Section 5 of the Securities Act divides the registration process into three periods: (1) the pre-filing period (i.e., the period after the decision to make an offering has been made, but before the registration statement is publicly filed, also referred to as the “quiet period”); (2) the waiting period (i.e., the period after the registration statement is publicly filed but before it is declared effective); and (3) the post-effective period (i.e., the period after the registration statement becomes effective).³

During the pre-filing period, Section 5(c) of the Securities Act prohibits all “offers,” interpreted broadly (see 3.(a) below).

After the registration statement is publicly filed (i.e., during the waiting period and post-effective period), Section 5(b)(1) of the Securities Act prohibits any “prospectus,” which includes all written or broadcast communications to be used in connection with a securities offering, unless it is a statutory prospectus that meets certain information and form

³ However, as discussed below, there is no waiting period for well-known seasoned issuers (“WKSIs”) using automatic shelf registration because “automatic shelf registration statements” become effective immediately upon filing (i.e., without SEC review).

requirements (i.e., unless it is a prospectus that meets the requirements of Section 10 of the Securities Act). Subject to two exceptions, a “prospectus” is defined in Section 2(a)(10) of the Securities Act to mean any prospectus, notice, circular, advertisement, letter or communication, written or by radio or television, which offers any security for sale or confirms the sale of any security. The first exception from the definition of “prospectus” is for certain limited written communications related to a securities offering for which a registration statement has been filed (see Rule 134 under the Securities Act, which is discussed below). Under the second exception, sales literature may be used during the post-effective period, even if it does not meet the requirements of Section 10, if it is sent after or with a prospectus that meets the requirements of Section 10(a) of the Securities Act (i.e., a “final prospectus”). Sales literature covered by the second exception is known as “supplemental sales literature.”

Section 5(a) of the Securities Act prohibits the sale or delivery of any security unless a registration statement has become effective for the security (i.e., until the post-effective period). And, Section 5(b)(2) of the Securities Act requires that any security being sold must be accompanied or preceded by a complete Section 10(a) prospectus (i.e., a final prospectus). Sections 5(b)(2) and 5(b)(1) of the Securities Act work together with Rule 10b-10 under the Exchange Act (the “confirmation rule”) and the definition of “prospectus” in Section 2(a)(10) of the Securities Act to require that, absent an exemption, a purchaser will receive a final prospectus at or before completion of the transaction.

Until the later of (1) completion of “distribution” of the securities (i.e., when the securities have been sold to investors), and (2) expiration of the relevant subsequent prospectus-delivery period, limitations on publicity by the issuer remain in place.

2. Special Considerations for Foreign Issuers, Including Offshore Press Activities

Under SEC interpretive guidance (or the safe harbors provided by Rules 168 and 169 under the Securities Act, which are discussed below), a foreign issuer may advertise its products and services, release customary shareholder reports, issue press releases concerning material business developments and respond to legitimate unsolicited requests for factual information about its affairs. However, until the U.S. offering has been completed, a foreign issuer should not schedule meetings or calls with U.S. securities analysts or similar groups: (a) that would be atypical in light of the issuer’s past practices, or (b) in which it would be hard to avoid questions and conjecture about the offering. The issuer should avoid: (a) conducting public relations activities within the United States that are atypical in light of the issuer’s past practices and the nature of the information being communicated; and (b) initiating, or cooperating in the preparation of, any press report in the United States about the issuer or its important officers that is atypical in light of the issuer’s past practices and the nature of the information being communicated. Additionally, publicity about the issuer that is issued in the United States in the normal course of business should avoid optimistic predictions, and press conferences in the United States should be avoided throughout the distribution process unless required because of other developments affecting the issuer.

Outside the United States, a foreign issuer may conduct, consistent with its past practices, customary disclosure, announcements and publicity activities. However, even customary activities in its home market should not be conducted where such activities might be

interpreted as intended to, or likely to, condition the U.S. market for the securities being offered. The SEC's publicity rules (discussed below) can be an important issue in global offerings that include a U.S. public offering, especially for issuers that are not required to file reports under the Exchange Act ("non-reporting issuers"), mainly because other jurisdictions do not impose such strict limitations. Therefore, issuers and underwriters must be careful to ensure that publicity permitted elsewhere does not enter the United States and result in a violation of these rules.

Rule 135e under the Securities Act provides a safe harbor for certain offshore press activity from the registration requirement of Section 5 of the Securities Act and is discussed below.

3. Permitted Publicity

(a) The Pre-Filing Period. The pre-filing period begins when an issuer decides to make a public offering in the United States (usually by retaining an investment bank to undertake the offering) and ends when the registration statement for the offering is first filed publicly with the SEC. During this period the issuer (and other offering participants) may not make offers or sales of the securities being registered. Consequently, during the pre-filing period, a publicity campaign related to the offering is prohibited. (This includes interviews related to the Company.)

Under Section 2(a)(3) of the Securities Act, the term "offer" includes any attempt or offer to dispose of a security for value. The SEC has construed the concept of offers broadly to prohibit publicity that does not refer to the proposed offering but that may stimulate investor or dealer interest in the issuer or its securities. The broadest prohibitions are in effect during the pre-filing period.

The SEC has provided safe harbors from Section 5(c)'s prohibition on pre-filing offers. For example, an issuer may:

1. release a limited notice concerning the offering within the United States under Rule 135 under the Securities Act;
2. if a foreign private issuer, conduct certain press activities outside the United States under Rule 135e under the Securities Act;
3. if a well-known seasoned issuer ("WKSI"), make offers of securities under Rule 163 under the Securities Act;
4. take advantage of the 30-day safe harbor for certain pre-filing statements under Rule 163A under the Securities Act;
5. if a non-reporting issuer, continue to release certain factual business information under Rule 169 under the Securities Act; and
6. if a reporting issuer or a qualifying non-reporting foreign private issuer, continue to release certain factual business information and forward-looking information under Rule 168 under the Securities Act.

Additionally, as discussed later:

- a broker-dealer that has not participated, is not participating, and will not be participating, in the distribution may publish research reports that comply with Rule 137 under the Securities Act; and
- a broker-dealer that will be, or is, participating in the distribution may publish research reports that comply with Rule 138 or 139 under the Securities Act.

(i) Rule 135: Limited Announcement

Rule 135 permits an issuer or a selling security holder (and any person acting on behalf of either of them) to make a public announcement of a planned registered offering during the pre-filing period if the announcement: (A) contains a legend to the effect that it does not constitute an offer of any securities for sale; and (B) contains only limited information, including: (1) the name of the issuer; (2) the title, amount and basic terms of the securities to be offered; (3) the amount of securities to be offered by selling security holders (if any); (4) the anticipated timing of the offering; (5) a brief statement of the manner and purpose of the offering without naming the prospective underwriters for the offering; (6) whether the issuer is directing its offering to only a particular class of purchasers; (7) any legend or statement required by state or foreign country law or administrative authority; and (8) certain additional information for rights offerings, exchange offers, Rule 145(a) offerings (certain reclassifications of securities, mergers, consolidations and acquisitions of assets) and offerings to employees.

(ii) Rule 135e: Offshore Press Conferences and Materials

Rule 135e provides a safe harbor from the U.S. publicity restrictions for certain offshore press activities by foreign issuers. Rule 135e permits a foreign private issuer or foreign government issuer, a selling security holder of such an issuer, or their representatives (including underwriters and public relations firms) to provide journalists, U.S. or foreign, with access to press conferences held outside the United States, to meetings with issuer or selling security holder representatives conducted outside the United States, or to written press-related materials released outside the United States, at or in which a proposed or present offering of securities is discussed, if certain conditions are met. Press activities permitted by Rule 135e are not “offers” under Section 5 and, therefore, are not: (A) pre-filing offers in violation of Section 5(c), or (B) nonconforming prospectuses (i.e., illegal written offers) during the waiting or post-effective period in violation of Section 5(b)(1). The availability of the Rule 135e safe harbor is subject to the following conditions: (A) the relevant press activity (described above) occurs offshore; (B) the proposed or present offering is not intended to be conducted solely in the United States; (C) access to the offshore press activity is provided to both U.S. and foreign journalists; and (D) any written press releases or other press-related materials released to journalists: (1) contain a legend stating that the materials are not an offer of securities for sale in the United States (as well as certain other information), and (2) do not include any mail-in coupon or similar form that prospective purchasers could return to indicate their interest in the offering.

(iii) Rule 163: Pre-Filing Offers by WKSIs

Rule 163 provides an exemption for all pre-filing communications by “WKSIs” (defined below) from the prohibition in Section 5(c) of the Securities Act on offers before a registration statement has been filed. Rule 163 permits WKSIs to make unrestricted oral and written offers before filing a registration statement (i.e., those offers will not violate Section 5(c)). However, any written offer made under the exemption will be considered a “free writing prospectus” of the issuer and generally will have to be filed upon the filing of a registration statement or amendment covering the securities. As discussed below, “free writing prospectuses” are generally written offers other than a permitted preliminary or final statutory prospectus.

The Rule 163 exemption is subject to the following conditions:

- (A) By or on behalf of the issuer. The exemption applies only to offers “by or on behalf of” the issuer (a communication is made “by or on behalf of” an issuer if the issuer or an agent or representative of the issuer, other than an offering participant who is an underwriter or dealer,⁴ authorizes or approves the communication before it is made);
- (B) Intended to be registered. The exemption applies to an offering by or on behalf of a WKSI that will be or is at the time intended to be registered under the Securities Act;
- (C) Filing. Every written offer made in reliance on the exemption must be filed by the issuer with the SEC “promptly” upon the filing of the registration statement (if one is filed) or an amendment (if one is filed) covering the securities that have been offered under the exemption. Accordingly, if no such registration statement or amendment is filed, the free writing prospectus need not be filed. Additionally, the Rule 163 filing condition does not apply to any communication: (1) that was previously filed with, or furnished to, the SEC (e.g., under Regulation FD or on Form 8-K);⁵ or (2) that the issuer would not be required to file with the SEC under the conditions of Rule 433 under the Securities Act (the free writing prospectus rule) if the communication was a free writing prospectus used after the filing of the registration statement.⁶ Finally,

⁴ See H.1. below for a discussion of participating dealers.

⁵ Regulation FD is discussed in Chapters 6 and 9. Form 8-K is discussed in Chapter 9.

⁶ Rule 433 is discussed later in this Chapter.

the Rule 163 filing condition will be met if the issuer meets the filing conditions (other than timing of filing, which is provided in Rule 163) that would apply under Rule 433 if the communication was a free writing prospectus used after the filing of the registration statement. As a result, the accommodations provided in Rule 433 concerning media publications that are free writing prospectuses also apply under Rule 163;⁷

- (D) Legend. Every written offer made in reliance on the exemption must contain substantially the following legend: “The issuer may file a registration statement (including a prospectus) with the SEC for the offering to which this communication relates. Before you invest, you should read the prospectus in that registration statement and other documents the issuer has filed with the SEC for more complete information about the issuer and this offering. You may get these documents for free by visiting EDGAR on the SEC Web site at www.sec.gov. Alternatively, the company will arrange to send you the prospectus after filing if you request it by calling toll-free 1-8[xx-xxx-xxxx].” The legend also: (1) may provide an e-mail address at which the documents can be requested, and (2) may indicate that the documents also are available by accessing the issuer’s web site and provide the Internet address and the particular location of the documents on the web site;⁸
- (E) Liability. While communications covered by Rule 163 are exempt from the U.S. publicity restrictions (i.e., from Section 5(c)’s prohibition on pre-filing offers), these communications are still considered offers and remain subject to the U.S. liability standards applicable to offers,

⁷ An immaterial or unintentional failure to file or delay in filing a free writing prospectus will not result in a violation of Section 5(c) or loss of the ability to rely on the exemption if: (1) a good faith and reasonable effort was made to comply with the filing condition, and (2) the free writing prospectus is filed as soon as practicable after discovery of the failure to file.

⁸ An immaterial or unintentional failure to include the specified legend will not result in a violation of Section 5(c) or loss of the ability to rely on the exemption if: (1) a good faith and reasonable effort was made to comply with the specified legend condition, (2) the free writing prospectus is amended to include the specified legend as soon as practicable after discovery of the omitted or incorrect legend, and (3) if the free writing prospectus was transmitted without the specified legend, it is retransmitted with the legend by substantially the same means as the original free writing prospectus and directed to substantially the same prospective purchasers to whom the free writing prospectus was originally transmitted.

including the anti-fraud provisions of the U.S. federal securities laws;⁹

- (F) Subject to Regulation FD. Communications made under this exemption are subject to Regulation FD; specifically, communications made under Rule 163 cannot rely on the exclusion from Regulation FD for statements made in connection with a registered securities offering;
- (G) Excluded communications. Rule 163's exemption from Section 5(c) is not available for: (1) communications relating to business combination transactions that are subject to Rule 165 or 166 under the Securities Act (however, Rule 165 provides the offeror with an exemption from Section 5(c) if certain conditions are met); or (2) communications by an issuer that is a registered investment company or a business development company.

(iv) Rule 163A: A 30-Day Bright Line Safe Harbor

Rule 163A permits all issuers (whether or not WKSIs) to make certain communications more than 30 days before the filing of a registration statement and these communications are not deemed to be offers for Section 5(c) or free writing prospectuses. The SEC adopted Rule 163A to clarify the application of the Securities Act to an issuer's pre-filing communications that might not fall within the Rule 168 and 169 safe harbors for regularly released factual business and forward-looking information (which are discussed later).

The 30-day safe harbor of Rule 163A is subject to the following conditions:

- (A) No reference to the securities offering. The communication must not refer to the securities offering that is the subject of the registration statement;
- (B) By or on behalf of the issuer. The communication must be made "by or on behalf of" the issuer (even an IPO issuer), not other offering participants such as underwriters or dealers;
- (C) No further distribution. The issuer must take reasonable steps within its control to prevent further distribution or publication of the information during the 30-day period before filing the registration statement (although the SEC has suggested that the issuer may maintain this information

⁹ The anti-fraud provisions of the U.S. federal securities laws are discussed in Chapters 14 and 15.

on its web site if the information is appropriately dated, otherwise identified as historical material and not referred to as part of the offering activities);¹⁰

- (D) Regulation FD and liability. Statements made in reliance on Rule 163A are still subject to Regulation FD, other disclosure requirements, and the anti-fraud provisions of the U.S. federal securities laws;¹¹
- (E) Excluded offerings and issuers. The 30-day safe harbor is not available for communications relating to: (1) business combination transactions that are subject to Rule 165 or Rule 166 under the Securities Act, including exchange offers (however, Rule 166 provides that any communication relating to a business combination transaction made before the first public announcement of the transaction will not be an “offer” under Section 5(c), so long as the participants take all reasonable steps within their control to prevent further distribution or publication of the communication until either the first public announcement is made or the registration statement related to the transaction is filed); (2) offerings registered on Form S-8 under the Securities Act (for employee benefit plans), unless the issuer is a WKSI; or (3) offerings of securities of an issuer that is, or during the past three years was (or any of whose predecessors during the last three years was) a blank check company, a shell company (other than a business combination related shell company) or an issuer for an offering of penny stock. Additionally, the 30-day

¹⁰ While the SEC does not expect an issuer to be able to control the republication or accessing of previously published press releases, the SEC does expect issuers and persons acting on their behalf to be able to control their own involvement in any later redistribution or publication. For example, if an issuer or its representative gives an interview to the press before the 30-day period, it will not be able to rely on Rule 163A if the interview is published during the 30-day period. Presumably, the SEC means that an issuer must obtain an agreement that the interview will not be published during the 30-day period.

¹¹ While communications covered by Rule 163A will not be an “offer” for Section 5(c), those communications are not excluded from the definition of “offer” for other purposes under the Securities Act, including the definition of “prospectus” in Section 2(a)(10) of that Act. In contrast, Rules 168 and 169 also exclude the release of permissible factual business information and forward-looking information from the definition of “prospectus” in Section 2(a)(10). Accordingly, unlike communications covered by Rule 168 or 169, communications falling only within Rule 163A are subject to disclosure liability under Section 12(a)(2) of the Securities Act. (Section 12(a)(2) provides an express private right of action to any purchaser of a security that proves the security was offered or sold (through use of the jurisdictional means) by means of a prospectus or oral communication that contained a false statement of material fact or omitted a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission). For an oral communication to be subject to Section 12(a)(2), it must relate to a prospectus.)

safe harbor is not available for communications made by an issuer that is a registered investment company or a business development company.

(v) Rules 168 and 169: Factual Business Information and Forward-Looking Information During An Offering

Issuers may continue to advertise products and services and issue press releases concerning factual business and financial developments in accordance with past practice, despite the limitations on publicity.

In 1971, to encourage the flow of factual information to shareholders and investors even during a distribution, the SEC issued some broad guidelines to issuers. The SEC stated that, when in registration, issuers should: (A) continue to advertise products and services; (B) continue to send out customary quarterly, annual and other periodic reports to stockholders; (C) continue to publish proxy statements and send out dividend notices; (D) continue to make announcements to the press concerning factual business and financial developments (i.e., receipt of a contract, the settlement of a strike, the opening of a plant or similar events of interest to the community in which the business operates); (E) answer unsolicited telephone inquiries from stockholders, financial analysts, the press and others concerning factual information; (F) observe an "open door" policy in responding to unsolicited inquiries concerning factual matters from securities analysts, financial analysts, security holders and participants in the communications field who have a legitimate interest in the corporation's affairs; and (G) continue to hold stockholder meetings as scheduled and to answer shareholders' inquiries at stockholder meetings relating to factual matters. The SEC also stated that, to curtail problems in this area, issuers should avoid: (1) issuance of forecasts, projections or predictions relating but not limited to revenues, income or earnings per share; and (2) publishing opinions concerning values.

However, in 2005, the SEC adopted safe harbors from the publicity restrictions that codified and, for certain issuers, expanded, the exclusions discussed in (A) through (G) above. These safe harbors are contained in Rules 168 and 169 under the Securities Act.

Rules 168 and 169 permit certain information regularly released by or on behalf of an issuer in the ordinary course of its business. These communications are not "offers" under Section 5(c) or "prospectuses" under Section 2(a)(10). Therefore, they are not free writing prospectuses (i.e., written offers other than a statutory prospectus).

Rule 168 permits a reporting issuer and certain non-reporting foreign private issuers to make the continued regular release or dissemination of "factual business information" and "forward-looking information," subject to certain conditions. For Rule 168, "factual business information" is some or all of the following types of information, including if contained in any report or other materials that the issuer files with, furnishes to or submits to the SEC under the Exchange Act: (A) factual information about the issuer, its business or financial developments or other aspects of its business; (B) advertisements of, or other information about, the issuer's products or services; and (C) dividend notices. For Rule

168, “forward-looking information” is some or all of the following types of information, including if contained in any report or other materials that the issuer files with, furnishes to or submits to the SEC under the Exchange Act: (A) projections of the issuer's revenues, income (loss), earnings (loss) per share, capital expenditures, dividends, capital structure or other financial items (including, for example, earnings expectations and guidance information); (B) statements about management's plans and objectives for future operations, including plans or objectives for products or services of the issuer; (C) statements about the issuer's future economic performance, including statements of the type contemplated by management's discussion and analysis of financial condition and results of operations (“MD&A”);¹² and (D) assumptions underlying or relating to any of the above information. However, neither term includes information about an offering or information released or disseminated as part of offering activities. Disclosure of Rule 168 information is permitted at any time, including before and after the filing of a registration statement.

Rule 169 permits non-reporting issuers to make the continued regular release or dissemination of factual business information, but not forward-looking information, subject to certain conditions. One condition is that the factual business information: (A) must be released for intended use by persons, such as customers and suppliers, other than in their capacities as investors or potential investors in the issuer's securities; and (B) must be released by the issuer's employees or agents who historically have provided such information. This condition does not apply under Rule 168. Additionally, the definition of “factual business information” is narrower under Rule 169 than under Rule 168 (i.e., for Rule 169, “factual business information” is some or all of the following types of information: (A) factual information about the issuer, its business or financial developments or other aspects of its business; and (B) advertisements of, or other information about, the issuer's products or services). But under both Rules, factual business information does not include information about an offering or information released or disseminated as part of offering activities. Rule 169 information may be released at any time, including before or after the filing of a registration statement.

Rules 168 and 169 provide an exemption only from Section 5 of the Securities Act. Consequently, factual business information (and forward-looking information) released by reporting issuers continues to be subject to: (A) Regulation FD (which prohibits the selective disclosure by issuers of material non-public information); (B) Regulation G (which governs the use of non-GAAP financial measures in public disclosures); (C) Item 10 of Regulation S-K (which explains the SEC's policy on projections of future economic performance, securities ratings and the use of non-GAAP financial measures in SEC filings); and (D) Item 2.02 of Form 8-K (which covers disclosure of earnings information for a completed fiscal period).

In general, as the SEC recognized many years ago, ordinary factual business communications that an issuer regularly releases are not considered an “offer” of securities and, therefore, do not violate Section 5. The safe harbors discussed in this section do not affect in any way the Securities Act analysis concerning ordinary course business

¹² MD&A disclosure is discussed in Chapter 12.

communications that are not within the safe harbors. Accordingly, ordinary course business communications that are not within the safe harbors will not be presumed to be offers, and whether they are offers will depend on the facts and circumstances.

(b) The Waiting Period.

During the waiting period (i.e., after the registration statement is publicly filed, but before it is declared effective), sales of the securities continue to be prohibited. However, during this period, some communications are permitted (and even necessary to market the offering): a sales pitch by securities salesmen, seminars and “road shows” (defined below). An internal memorandum for underwriters is permitted but distribution must be limited.

Basically, there are six types of offers that are permitted to be made during the waiting period: (1) oral offers; (2) tombstone ads and other written communications permitted under Rule 134 (these communications are not “prospectuses” under Section 2(a)(10)); (3) preliminary prospectuses under Rule 430 (called a “red herring”); (4) summary prospectuses under Rule 431 under the Securities Act (or Rule 498 under that Act, for mutual funds);¹³ (5) the complete Section 10(a) statutory prospectus (i.e., the final prospectus), if it is available (as it may be where a firm commitment underwriting is not used); and (6) free writing prospectuses (generally, written offers other than a statutory prospectus) under Rules 164 and 433 under the Securities Act. Depending on the circumstances, a road show will be either an oral offer or a free writing prospectus.¹⁴ Where an internal memorandum for underwriters is inadvertently distributed to a potential investor, it may be possible to treat the communication “after-the-fact” as a free writing prospectus and thereby avoid violating the publicity restrictions.

Communications Permitted After Filing a Registration Statement:

(A) Oral Communications; and

¹³ Summary prospectuses are rarely used except where the issuer is a mutual fund.

¹⁴ During the waiting period, the underwriting group “pre-sells” (i.e., obtains “indications of interest” for) the offering. This process is commonly referred to as “bookbuilding.” Issuers and underwriters often conduct presentations known as “road shows” to market their offerings to the public. Road shows are a primary means by which issuers are involved directly and actively in the selling effort to investors. Specifically, the managing underwriter often organizes a road show, which consists of a series of meetings held across the United States (and often outside the United States) at which the issuer’s management delivers presentations to selected groups of investment advisers, institutional investors and securities salesmen. Management also answers questions and makes available preliminary prospectuses at the road show. However, by 2005, road shows also were being conducted or re-transmitted over the Internet or other electronic media and in some cases to broader audiences. In 2005, the SEC revised the treatment of electronic road shows (see the next footnote). Now, the transmission of electronic road shows is permitted, provided that the conditions concerning use of free writing prospectuses applicable to electronic road shows are met. Besides securing indications of interest, the road show also helps the managing underwriter price the offering.

(B) “Written Communications” (including “graphic communications”), both as defined in Rule 405 under the Securities Act;¹⁵ however, as discussed later, written communications that are free writing prospectuses generally must be:

- accompanied or preceded by a statutory prospectus (including a price range in an IPO) where the issuer is a non-reporting issuer or an unseasoned issuer; and
- filed with the SEC on or before the date of first use.

Oral offers are permitted, i.e., they do not violate Section 5, but if they are false or misleading, they may cause liability under Sections 12(a)(2) and 17(a) of the Securities Act and Rule 10b-5 under the Exchange Act.

The SEC has provided safe harbors from the publicity restrictions of the waiting period (i.e., from Section 5(b)(1)’s prohibition on written offers other than a statutory prospectus). For example, an issuer may:

1. if a non-reporting issuer, continue to release certain factual business information under Rule 169;
2. if a reporting issuer or a qualifying non-reporting foreign private issuer, continue to release certain factual business information and forward-looking information under Rule 168;
3. if a foreign private issuer, conduct certain press activities outside the United States under Rule 135e; and
4. make a limited written notice within the United States under Rule 134. The Rule 134 safe harbor is available to any party (e.g., an underwriter).

¹⁵ Under Section 2(a)(10) of the Securities Act, a “prospectus” is “any . . . communication, written or by radio or television” that offers a security for sale or confirms the sale of a security (except for: (1) Rule 134 communications; and (2) supplemental sales literature (i.e., sales literature sent or given during the post-effective period, if accompanied or preceded by a final prospectus)). Section 2(a)(9) of the Securities Act, in turn, defines “written” to include “any means of graphic communication.” In 2005, the SEC adopted new definitions of “written communication” and “graphic communication.” Rule 405 under the Securities Act now defines a “written communication” as any communication that is written, printed, television or radio broadcast (regardless of transmission means) or a graphic communication. The definition excludes oral communications, such as live telephone calls, but broadly disseminated oral communications, such as “blast” voice mail messages, are considered similar to broadcasts and are, therefore, written communications. A “graphic communication” includes any form of electronic media, such as audiotapes, videotapes, facsimiles, CD-ROM, e-mail, Internet web sites, and computers, computer networks and other forms of computer data compilation. A graphic communication does not include a communication that, when it originates, it is live, in real-time to a live audience, and does not originate in recorded form or otherwise as a graphic communication, even if it is transmitted through a graphic communication. The definition of graphic, and therefore written, communication now clearly excludes live road shows that are transmitted in real-time over the Internet or to overflow rooms. Thus, Rule 405 now makes it clear that all electronic communications (other than telephone and other live, in real-time communications to a live audience) are graphic and, therefore, written communications for the Securities Act.

Additionally, as discussed later:

- a broker-dealer that has not participated, is not participating, and will not be participating, in the distribution may publish research reports that comply with Rule 137; and
- a broker-dealer that will be, or is, participating in the distribution may publish research reports that comply with Rule 138 or 139.

(i) Rule 134: Limited Written Communications

Rule 134 permits certain limited written communications related to a securities offering for which a registration statement has been filed (unless the issuer is a registered investment company or a business development company). Generally, the Rule 134 safe harbor provides that a written communication: (1) may include only the items of information permitted by the Rule, and (2) must include a specified cautionary legend and the name and address of a person or persons from whom a prospectus meeting the requirements of Section 10 of the Securities Act, other than a free writing prospectus (i.e., a statutory prospectus) may be obtained. A written communication that meets these criteria is deemed not to be a “prospectus” under Section 2(a)(10) or a “free writing prospectus” and can be published or transmitted by any party to any person after the registration statement has been filed (i.e., during the waiting period or post-effective period) without violating Section 5(b)(1).

Rule 134 is not available until a preliminary prospectus (or, in the case of shelf registration, which is discussed later, a base prospectus) has been filed with the SEC. Additionally, for a non-reporting issuer (generally, for an issuer’s IPO in the United States), information related to the pricing, final maturity, interest rate, yield and rating of the security (specifically, the information specified in items (D), (E), (F) and (Q) below) may be included in a Rule 134 notice only if the prospectus that is part of the filed registration statement (i.e., the statutory prospectus) includes a price range.¹⁶ Accordingly, in an IPO, most of the information permitted by Rule 134 may be included in a Rule 134 notice before the statutory prospectus includes a price range.

Currently, a Rule 134 notice may include the following items of information:¹⁷

¹⁶ See B.2.(b)(i) above. Note that it is not necessary to circulate the preliminary prospectus to rely on Rule 134 for the information specified in items (D), (E), (F) and (Q) below. To rely on Rule 134 for that information, it is only necessary that, in an IPO, a preliminary prospectus has been filed that includes a price range (i.e., that, in an IPO, a preliminary prospectus that includes a price range is available). In an IPO, the initial filing with the SEC frequently will not include a price range. In many cases, the price range is not included in registration statements for IPOs until a later point in time that is closer to the commencement of marketing activities for the offering.

¹⁷ Originally, Rule 134 was intended to permit an “identifying statement” that could be used to locate persons that might be interested in receiving a statutory prospectus. Rule 134 was adopted under Section 2(a)(10)(b) of the Securities Act, which excludes from the definition of “prospectus” in Section 2(a)(10):

- (A) factual information about the legal identity and business location of the issuer, limited to: (1) the issuer's name; (2) the address, phone number and e-mail address of the issuer's principal offices and contact for investors; (3) the issuer's country of organization; and (4) the geographic areas in which the issuer conducts business;
- (B) a brief indication of the general type of business of the issuer, limited to: (1) for a manufacturing company, the general type of manufacturing, the principal products or classes of products manufactured and the segments in which the company conducts business; (2) for a public utility company, the general type of services rendered, a brief indication of the area served and the segments in which the company conducts business; (3) for an asset-backed issuer, the identity of key parties, such as sponsor, depositor, issuing entity, servicer or servicers and trustee, the asset class of the transaction and the identity of any credit enhancement or other support; and (4) for any other type of company, a corresponding statement;
- (C) the title of the security (or securities) being offered and the amount (or amounts) being offered (the title may include a designation as to whether the securities are convertible, exercisable or exchangeable, and as to the ranking of the securities (i.e., senior or subordinated));
- (D) the price of the security or, if the price is not known, the method of its determination or the bona fide estimate of the price range as specified by the issuer or the managing underwriter or underwriters;
- (E) for a fixed income security, the final maturity and interest rate provisions or, if the final maturity or interest rate

a notice, circular, advertisement, letter, or communication in respect of a security . . . if it states from whom a [statutory prospectus] may be obtained and, in addition, does no more than identify the security, state [its price], state by whom orders will be executed, and contain such other information as the [SEC], by rules or regulations deemed necessary or appropriate in the public interest and for the protection of investors, and subject to such terms and conditions as may be prescribed therein, may permit.

In 2005, the SEC expanded the information permitted under Rule 134 “to include information that issuers, underwriters and investors will find helpful and to permit the types of written communications during an offering that [the SEC does] not consider raise the risk of offering abuses.” Although expanded, the amount of information about the issuer and the offering that may be included in a Rule 134 notice is still limited. For example, a Rule 134 notice still cannot be used to provide a detailed description of the securities being offered, such as a term sheet. However, term sheets can be distributed under the free writing prospectus rules discussed later.

provisions are not known, the probable final maturity or interest rate provisions, as specified by the issuer or the managing underwriter or underwriters;

- (F) for a fixed income security with a fixed (non-contingent) interest rate provision, the yield or, if the yield is not known, the probable yield range, as specified by the issuer or the managing underwriter or underwriters and the yield of fixed income securities with comparable maturities and credit ratings as referred to in (Q) below (yield disclosure may include disclosure of the anticipated spread over a benchmark);
- (G) a brief description of the intended use of proceeds of the offering, if this information is already disclosed in the prospectus that is part of the filed registration statement;
- (H) the name, address, phone number and e-mail address of the sender of the communication and the fact that it is participating, or expects to participate, in the distribution of the security;
- (I) the type of underwriting, if this information is already disclosed in the prospectus that is part of the filed registration statement;
- (J) the names of all underwriters participating in the offering and their additional roles, if any, within the underwriting syndicate (e.g., lead book-running manager);
- (K) the anticipated schedule for the offering (including the approximate date on which the proposed sale to the public will begin) and a description of marketing events, such as road shows (including the dates, times, locations and procedures for attending or otherwise accessing the events);
- (L) a description of the procedures by which the underwriters will conduct the offering and the procedures for transactions in the offering with the issuer or an underwriter or participating dealer (including procedures for account-opening and submitting indications of interest and conditional offers to buy the offered securities, but not written notices of allocations of securities), and the procedures for directed share plans and other participation in offerings by officers, directors and employees of the issuer;

- (M) whether, in the opinion of counsel, the security is a legal investment for savings banks, fiduciaries, insurance companies or similar investors under the laws of any state or territory or the District of Columbia, and the permissibility or status of the investment under the Employee Retirement Income Security Act of 1974 (ERISA);
- (N) whether, in the opinion of counsel, the security is exempt from specified taxes, or the extent to which the issuer has agreed to pay any tax with respect to the security or measured by the income therefrom;
- (O) whether the security is being offered through rights issued to security holders (i.e., whether the offering is a rights offering) and, if so, the class of securities the holders of which will be entitled to subscribe, the subscription ratio, the actual or proposed record date, the date on which the rights were issued or are expected to be issued, the actual or anticipated date on which they will expire and the approximate subscription price, or any of the above;
- (P) any statement or legend required by state law or administrative authority;
- (Q) regarding the securities being offered: (1) any security rating assigned, or reasonably expected to be assigned, by a nationally recognized statistical rating organization (“NRSRO”) (as defined in Rule 15c3-1(c)(2)(vi)(F) under the Exchange Act) and the name of the NRSRO that assigned or is reasonably expected to assign the rating; and (2) if registered on Form F-9, any security rating assigned, or reasonably expected to be assigned, by any other rating organization specified in the Instruction to General Instruction I.A(2) of Form F-9;¹⁸
- (R) the names of selling security holders, if this information is already disclosed in the prospectus that is part of the filed registration statement;
- (S) the names of securities exchanges or other securities markets where any class of the issuer's securities are, or will be, listed;

¹⁸ Form F-9 is discussed in the next chapter.

- (T) the ticker symbols, or proposed ticker symbols, of the issuer's securities;
- (U) the CUSIP number (as defined in Rule 17Ad-19(a)(5) under the Exchange Act) assigned to the securities being offered; and
- (V) information disclosed to correct inaccuracies previously contained in a communication permissibly made under Rule 134.

Additionally, unless a Rule 134 notice: (I) does no more than state from whom, and include the uniform resource locator (“URL”) address where, a statutory prospectus may be obtained, identify the security, state its price and state by whom orders will be executed, or (II) is accompanied or preceded by a statutory prospectus (including a price range where required), the notice must contain specified information. The specified information is as follows: (1) if the registration statement has not yet become effective, the following legend: “A registration statement relating to these securities has been filed with the Securities and Exchange Commission but has not yet become effective. These securities may not be sold nor may offers to buy be accepted prior to the time the registration statement becomes effective”; and (2) the name and address of a person or persons from whom a statutory prospectus (including as to the identified items above (i.e., items (D), (E), (F) and (Q)) a price range where required), may be obtained.

A Rule 134 notice may be used to solicit an indication of interest or an offer to buy if it: (I) is accompanied or preceded by a statutory prospectus (including a price range where required), and (II) contains substantially the following legend: “No offer to buy the securities can be accepted and no part of the purchase price can be received until the registration statement has become effective, and any such offer may be withdrawn or revoked, without obligation or commitment of any kind, at any time prior to notice of its acceptance given after the effective date.”¹⁹

The requirement that certain Rule 134 notices be accompanied or preceded by a statutory prospectus may be met in an electronic notice by including an active hyperlink to the statutory prospectus. However, the notice itself may not include information beyond that permitted by the Rule and, therefore, the notice may not include a hyperlink or URL for an address containing information beyond that permitted by Rule 134. For Rule 134, including a URL address to the statutory prospectus that is not an active hyperlink in an electronic communication does not mean that the statutory prospectus has been delivered. However, an active hyperlink to a statutory prospectus in an electronic Rule 134 notice will meet the requirement that the prospectus accompany or precede that notice.

Rule 134 notices need not be filed with the SEC. Because they are deemed not to be “prospectuses,” they are not subject to Section 12(a)(2) or Section 11 liability.

¹⁹ However, this legend need not be included in a notice to a dealer.

However, they are subject to potential anti-fraud liability under Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

In addition to notices, Rule 134 also applies to advertisements, circulars, letters or other communications published or transmitted by any person after the registration statement is filed, provided the conditions of the Rule are met. This includes press releases issued after the registration statement has been filed. Issuers often issue press releases after the registration statement is filed.

Under Rule 134, after the registration statement has been filed, the public offering may be advertised through a tombstone ad, which is a very limited advertisement. Tombstone ads (so named because of their extremely limited content) are announcements identifying the existence of a public offering and the availability of a statutory prospectus. While tombstone ads are permitted during the waiting period, they generally are used mainly to publicize a successful offering rather than to advertise offered securities and, therefore, are usually published the day after the registration statement is declared effective.

With limited exceptions, the SEC has taken the position that the inclusion of any information beyond that permitted by Rule 134 renders the Rule unavailable and, therefore, can result in the communication being deemed a “prospectus” (i.e., a written offer) that does not meet the requirements of Section 10 in violation of Section 5(b)(1). Accordingly, as a best practice, an announcement under Rule 134 should not be accompanied by any other announcement.

(ii) Free Writing Prospectuses

Generally, a “free writing prospectus” is any written communication that: (A) is an offer to sell or a solicitation of an offer to buy securities that are (or, for a well-known seasoned issuer, will be) the subject of a registration statement; and (B) does not meet the information and form requirements of a statutory prospectus. Since December 2005, free writing prospectuses may be used by all offering participants during the waiting period and post-effective period (and, by well-known seasoned issuers, even during the pre-filing period) if certain conditions are met. Free writing prospectuses (including electronic road shows) are discussed in detail in F. below.

(c) The Post-Effective Period.

Section 5(a) of the Securities Act prohibits the sale or delivery of a security unless a registration statement has become effective for the security (i.e., until the post-effective period). During the post-effective period, the only limitations on securities sales (other than the disclosure and anti-fraud provisions) are the prospectus delivery requirements of Section 5(b) of the Act (which are discussed in G.3. below).

Regarding offers, Section 5(b)(1) requires that, during the waiting and post-effective periods, all prospectuses (i.e., written offers to sell) meet the requirements of Section 10 of the Securities Act. Although the permissible offering methods are basically the same during the waiting and post-effective periods (e.g., oral offers and free writing prospectuses under Rules

164 and 433 are permitted during both periods), some methods by their nature are limited to the waiting period. For example, the preliminary prospectus under Rule 430 (the red herring) is expressly limited to the waiting period. Similarly, certain offering devices (e.g., supplemental sales literature and the Rule 430A prospectus, both of which are discussed below) are by their nature limited to the post-effective period.

The SEC has provided safe harbors from the publicity restrictions of the post-effective period (i.e., from Section 5(b)(1)'s prohibition on written offers other than a statutory prospectus). For example, an issuer may:

1. if a non-reporting issuer, continue to release certain factual business information under Rule 169;
2. if a reporting issuer or a qualifying non-reporting foreign private issuer, continue to release certain factual business information and forward-looking information under Rule 168; and
3. if a foreign private issuer, conduct certain press activities outside the United States under Rule 135e.

Additionally, as discussed later:

- a broker-dealer that has not participated, is not participating, and will not be participating, in the distribution may publish research reports that comply with Rule 137; and
- a broker-dealer that will be, or is, participating in the distribution may publish research reports that comply with Rule 138 or 139.

After the registration statement becomes effective, underwriters and other distribution participants may sell the securities only by means of a final prospectus. Additionally, there is a requirement for dealers to “deliver” a final prospectus during a period of time after effectiveness, even for aftermarket resales. Accordingly, restrictions on publicity by the issuer will remain in place until: (A) the distribution of the securities is completed (i.e., until the securities have been sold to investors), or (B) the relevant final prospectus delivery period expires, whichever occurs later. Once these periods have passed, offering-related restrictions on publicity generally can cease. (Additional considerations may apply where part of the securities were sold outside the United States under Regulation S, which is discussed in Chapter 8. In particular, if the periods in (A) and (B) above expire before the Regulation S “distribution compliance period” expires, publicity in the United States will continue to be prohibited until the Regulation S distribution compliance period has ended.)

(i) Supplemental Sales Literature

During the post-effective period, sales literature may be used if it is accompanied or preceded by a Section 10(a) (i.e., final) prospectus. Section 5(b)(1) prohibits the use of the mails or interstate facilities to send any prospectus after the filing date unless the prospectus meets the requirements of Section 10, and Section 2(a)(10) defines the term

prospectus as, basically, any written offer. Nonetheless, there are two exceptions to Section 2(a)(10)'s definition: (1) Rule 134 communications (excluded under Section 2(a)(10)(b)), and (2) supplemental sales literature (excluded under Section 2(a)(10)(a)). Specifically, Section 2(a)(10)(a) provides that:

a communication sent or given after the effective date of the registration statement (other than a prospectus permitted under [Section 10(b)]) shall not be deemed a prospectus if it is proved that prior to or at the same time with such communication a written prospectus meeting the requirements of [Section 10(a)] at the time of such communication was sent or given to the person to whom the communication was made.

Accordingly, sales literature may be used during the post-effective period, even if it does not meet the requirements of Section 10, if it is sent after or with a final prospectus.²⁰

This “supplemental sales literature” is not a free writing prospectus and, therefore, need not meet the filing or other conditions for the use of a free writing prospectus. Although supplemental sales literature generally need not be filed with the SEC, members of the Financial Industry Regulatory Authority, Inc. (“FINRA”) must file certain sales literature with FINRA.

Additionally, while there are no explicit statutory restrictions on the types of information that may be included in supplemental sales literature, such literature may not be misleading as it remains subject to the anti-fraud provisions of both the Securities Act and Exchange Act.

(ii) Rule 430A Prospectuses

Under Rule 430A under the Securities Act, in offerings for cash by any issuer, the prospectus contained in the registration statement at the time of effectiveness may omit the public offering price, other price-related information and certain other information, if

²⁰ Rule 172 under the Securities Act is not available to meet the condition to the exception in Section 2(a)(10)(a) that the final prospectus be “sent or given to the person to whom the communication was made.” As discussed later, Rule 172 provides that a final prospectus will be deemed to precede or accompany a security for sale for purposes of Section 5(b)(2) as long as the final prospectus is filed (or the issuer makes a good faith and reasonable effort to file it) with the SEC as part of the registration statement within the required Rule 424 prospectus filing timeframe. The SEC has clarified that a final prospectus only filed as provided in Rule 172 will not be considered to be “sent or given” before or with a written offer within the meaning of Section 2(a)(10)(a). Thus a significant limitation on the use of statutorily permitted supplemental sales literature during the post-effective period is that it must be proven by the person relying on the permissible use of such sales literature, that before or at the same time as receiving the sales literature, a final prospectus had been sent or given to the person receiving it.

the issuer furnishes the undertakings required by Item 512(i) of Regulation S-K.²¹ A Rule 430A prospectus may be used between effectiveness and pricing for purposes of making offers only (i.e., even though the registration statement is effective, because a Rule 430A prospectus contains no price terms, it is not considered a Section 10(a) or “final” prospectus). The price (and other) information omitted from a Rule 430A prospectus must be filed with the SEC after effectiveness in compliance with Rule 430A(a)(3).²²

(d) Research Reports.

Securities brokerage firms (broker-dealers), financial analysts and investment advisers face publicity issues similar to issuers for recommendations, research reports and market letters that relate to securities in registration. The publication or distribution by a broker-dealer of information, opinions or recommendations concerning an issuer or its securities (i.e., research reports) around the time of a registered offering can present issues under the publicity restrictions of the Securities Act, especially if the broker-dealer is or will be a participant in the distribution of the securities (i.e., an underwriter or selling group dealer).²³ In particular, such a report may constitute an offer to sell the securities and thus constitute an illegal offer if published or distributed before a registration statement is filed (i.e., during the pre-filing period), or it may constitute an illegal written offer to sell securities that does not meet the information requirements of Section 10 of the Securities Act if published or distributed after the registration statement is filed (i.e., during the waiting or post-effective period). To recognize the

²¹ Specifically, a Rule 430A prospectus may omit information concerning the public offering price, underwriting syndicate (including any material relationships between the issuer and underwriters not named in the prospectus), underwriting discounts or commissions, discounts or commissions to dealers, amount of proceeds, conversion rates, call prices and other items dependent upon the offering price, delivery dates and terms of the securities dependent upon the offering date. Like Rule 430 (concerning preliminary prospectuses), Rule 430A does not permit omission of the name of the managing underwriter(s). However, Rule 430A permits the issuer to omit the names of the other underwriters and certain related information.

²² The omitted price and other information may be included in a prospectus supplement filed with the SEC under Rule 424(b). See Securities Act Rule 430A(a)(3). This prospectus supplement must: (A) be filed within two business days after the earlier of the day the offering is priced or the day the prospectus containing the Rule 430A information is “first used” (i.e., available to the managing underwriter, syndicate members or offerees); or (B) be transmitted by a means reasonably calculated to result in filing with the SEC by that day. See Securities Act Rule 424(b)(1) and (4). However, if the prospectus supplement is not filed within 15 business days after the effective date of the registration statement (or any post-effective amendment to it), a post-effective amendment updated in all respects that either (A) restarts the 15-business-day period in which pricing must occur, or (B) contains the Rule 430A pricing and other information, must be filed and effective before sales are made and confirmations are sent. See Securities Act Rule 430A(a)(3). This post-effective amendment is effective on filing if the included prospectus contains no material changes from, or additions to, the prospectus previously filed as part of the effective registration statement (other than the price-related information omitted under Rule 430A).

Item 512(i) of Regulation S-K requires the issuer to undertake that, for determining liability under the Securities Act: (1) the information omitted from the Rule 430A prospectus and contained in a prospectus supplement filed under Rule 424(b)(1) or (4) is deemed to be part of the registration statement when it was declared effective; and (2) each post-effective amendment that contains a form of prospectus will be deemed to be a new registration statement for the securities offered, and the offering of the securities at that time will be deemed to be their initial bona fide offering. The undertaking in (1) above is intended to ensure that this information is subject to liability under Section 11 of the Securities Act.

²³ See H.1. below (discussing selling group dealers).

potential benefits of research reports while limiting their potential misuse to promote a securities offering, the SEC adopted Rules 137, 138 and 139 under the Securities Act (the “research safe harbors”) which set out the circumstances under which a broker-dealer may publish research contemporaneously with a registered offering without violating the publicity restrictions.

The research safe harbors apply throughout the distribution process (i.e., during the pre-filing, waiting and post-effective periods). Rule 137 provides a safe harbor for the publishing of research reports by broker-dealers that are not participating in an issuer’s registered distribution of securities (and have not participated, and do not propose to participate, in the distribution). Where the conditions of Rule 137 are met, the terms “offers,” “participates” or “participation” in Section 2(a)(11) of the Securities Act (i.e., the statutory definition of “underwriter”) will not apply to the broker-dealer’s publishing of research reports concerning the securities of an issuer that are the subject of an offering under a registration statement that the issuer proposes to file, has filed or is effective. Rules 138 and 139 provide safe harbors for the publishing of research reports by broker-dealers that are, or will be, participating in an issuer’s registered distribution of securities. Where the conditions of Rule 138 are met, a broker-dealer’s publishing of research reports about securities of an issuer other than those being distributed will not be “offers” under Sections 5(c) and 2(a)(10) of a security that is the subject of an offering under a registration statement that the issuer proposes to file, has filed or is effective. And, where the conditions of Rule 139 are met, a broker-dealer’s publishing of research reports about an issuer or any of its securities will not be “offers” under Sections 5(c) and 2(a)(10) of a security that is the subject of an offering under a registration statement that the issuer proposes to file, has filed or is effective. (However, to ensure that appropriate investor protections are maintained, the anti-fraud provisions of the U.S. federal securities laws, including Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, continue to apply to research reports issued under Rules 137, 138 and 139.)

Where a research report does not comply with any research safe harbor, it may be possible to treat the communication “after-the-fact” as a free writing prospectus and thereby avoid violating the publicity restrictions.

(i) Definition of Research Report

For the research safe harbors, a “research report” is a written communication that includes information, opinions or recommendations about securities of an issuer, or an analysis of a security or an issuer, whether or not it provides sufficient information for an investment decision.

(ii) Rule 137: Publication of Research by Non-Participating Broker-Dealers

Rule 137 permits a broker-dealer that was not, is not, and will not be, a participant in the registered offering to publish or distribute research. Rule 137:

- (A) applies to securities of any issuer, including non-reporting issuers (but excluding issuers that are or were, or whose predecessors were, during the preceding three years: blank

check companies, shell companies (other than business combination related shell companies) or penny stock issuers);

- (B) is available only to broker-dealers who have not received compensation from the issuer, selling security holders, participants in the securities distribution or any other person interested in the securities that are (or will be) the subject of the registration statement, for publishing or distributing the research (however, this does not preclude the broker-dealer from charging: (1) the regular price being paid by the broker-dealer for independent research, or (2) the regular subscription or purchase price for the research report); and
- (C) requires that the broker-dealer must publish or distribute the research report in the regular course of its business.

(iii) Rule 138: Publication of Research by an Underwriter (or Selling Group Member) on Other Securities of an Issuer

Rule 138 permits a broker-dealer that is or will be participating in a registered distribution of securities by a reporting issuer (or a qualifying non-reporting foreign private issuer) to publish or distribute research about a different type of security of that issuer than the securities registered, e.g., research by an underwriter on debt securities when participating in a distribution of the issuer's common stock, and vice versa.

Rule 138:

- (A) covers research reports on: (1) all reporting issuers that are current in their Exchange Act reporting for the past year or for such shorter time that they were reporting issuers (i.e., not just Form S-3 or F-3 eligible issuers),²⁴ and (2) non-reporting foreign private issuers that (I) meet all the requirements for eligibility to use Form F-3 other than the reporting history provisions, (II) either meet the \$75 million public float threshold in General Instruction I.B.1 of Form F-3 or are issuing non-convertible investment grade securities under General Instruction I.B.2 of Form F-3, and (III) either have equity securities trading on a "designated offshore securities market" (as defined in Regulation S) and have had them so traded for at least a year, or have a worldwide market value of their outstanding common equity held by non-affiliates (i.e., a "public float")

²⁴ Forms S-3 and F-3 are discussed in the next chapter.

of \$700 million or more (however, the Rule does not cover research reports on issuers that are or were, or whose predecessors were, during the preceding three years: blank check companies, shell companies (other than business combination related shell companies) or penny stock issuers); and

- (B) includes a requirement that the broker-dealer must have previously published or distributed, in the regular course of its business, research reports “on the types of securities in question” (i.e., on the types of securities that are the subject of the reports).

The latter condition is intended to prevent the broker-dealer from using research reports to circumvent Section 5 of the Securities Act and the free writing prospectus rules. However, the broker-dealer need not have a history of publishing or distributing research reports about the particular issuer or its securities.

(iv) Rule 139: Publication of Research About the Securities Being Offered by an Underwriter (or Selling Group Member)

Rule 139 permits a broker-dealer that is or will be participating in a registered offering to publish ongoing research about the issuer and its securities without being deemed to offer those securities by way of its research reports. Rule 139 research can be: (A) research reports concerning the issuer or any class of its securities (“issuer-specific reports”), or (B) more general reports covering an industry sector (“industry reports”). Rule 139 covers Form S-3 or F-3 eligible issuers that meet certain requirements for issuer-specific reports, all reporting issuers for industry reports and qualifying non-reporting foreign private issuers (see the discussion of Rule 138) for both types of reports. However, the Rule does not cover research reports about issuers that are or were, or whose predecessors were, during the preceding three years: blank check companies, shell companies (other than business combination related shell companies), or penny stock issuers.

Issuer-specific reports: (A) must be published by the broker-dealer in the regular course of its business, and (B) may not represent the initiation of publication of research about the issuer or its securities (or reinitiation of such publication following discontinuation). The broker-dealer must have previously published at least one research report on the issuer or its securities, or have published one such report following discontinuation of coverage. Accordingly, a report initiating (or reinitiating) coverage of an issuer cannot qualify for Rule 139’s safe harbor for issuer-specific reports. However, this safe harbor permits a broker-dealer to initiate coverage on a new class of an issuer’s securities as long as the broker-dealer: (A) has published at least one research report about the issuer or its securities, including a different class of securities; or (B) has published at least one such report after discontinuing coverage.

For industry reports, the following conditions must be met: (A) the research report must include similar information for a substantial number of issuers in the

issuer's industry or sub-industry, or contain a comprehensive list of securities currently recommended by the broker-dealer; (B) the analysis concerning the issuer or its securities must be given no materially greater space or prominence in the publication than that given to other securities or issuers; and (C) the broker-dealer must publish research reports in the regular course of its business and, at the time of publishing the research report, must be including similar information about the issuer or its securities in similar reports (i.e., the research report must contain similar types of information about the issuer or its securities as contained in prior reports). Additionally, for projections of an issuer's sales or earnings in an industry report: (D) the broker-dealer must have previously published projections on a regular basis to meet the "regular course of its business" condition; (E) at the time of publishing the research report, the broker-dealer must be publishing projections for that issuer; and (F) for (A) above, projections covering the same or similar periods must be included for either a substantial number of issuers in the issuer's industry or sub-industry or substantially all issuers represented in the comprehensive list of securities contained in the research report.

4. Remedies for Violations of the Publicly Restrictions ("Gun-Jumping")

It is important to comply with the U.S. publicity restrictions (i.e., with Section 5 of the Securities Act and the SEC's publicity rules discussed in this Chapter) because violations of those restrictions (called "gun-jumping") can have severe consequences for the issuer and other offering participants. The SEC may: (a) delay the effectiveness of the registration statement to allow the impact of the violation to dissipate (i.e., require a "cooling-off" period before the offering can be made); or (b) force an underwriter who has engaged in gun-jumping to withdraw as such. In very extreme cases, the SEC may refuse to declare the registration statement effective and thus cause the offering to be abandoned. Other possible effects of a determination by the SEC that gun-jumping has occurred are that: (a) sales to persons receiving the improper offer may be prohibited; (b) the SEC may require additional disclosures to be added to the statutory prospectus (e.g., it may require the issuer to include in the statutory prospectus and, therefore, incur the risk of prospectus-level liability for, statements attributed to the issuer in press articles); or (c) the SEC may bring an enforcement action against the violator (e.g., the issuer may be held liable for statements contained in publicity materials that are deemed to be an illegal "prospectus"). Additionally, under Section 12(a)(1) of the Securities Act, any purchaser of securities issued in violation of Section 5 can bring a rescission action against the issuer and require the issuer to repurchase the securities at the price at which they were sold (i.e., the purchaser gets a one-year put option). The SEC, in turn, may require an issuer to disclose in its statutory prospectus the existence of those rescission rights (i.e., to add a so-called "rescission risk factor" to the statutory prospectus).

F. Free Writing Prospectuses and Road Shows

1. Categories of Issuers

Like the other publicity rules, the rules for free writing prospectuses distinguish between four categories of issuers based on their size, presence in the marketplace and reporting history under the Exchange Act, i.e., well-known seasoned issuers, seasoned issuers, unseasoned issuers and non-reporting issuers. The degree of flexibility granted to issuers in their public communications depends on which category they fall under, with larger and more well-known

companies being granted greater flexibility in communicating during the registration process.

(a) Well-Known Seasoned Issuers (“WKSIs”)

WKSIs are the largest issuers that have an Exchange Act reporting history and are presumptively the most widely followed in the marketplace. A “WKSI” is defined as an issuer that:

- (i) meets the eligibility requirements for use of Form S-3 or F-3, the “short form” Securities Act registration statements which incorporate by reference the issuer information already made public in the issuer’s periodic Exchange Act reports (i.e., is required to file reports under Section 13(a) or 15(d) of the Exchange Act (including annual reports on Form 10-K or 20-F), has timely filed all required Exchange Act reports for the preceding 12 months²⁵ and has not committed specified dividend or debt defaults since the end of its last fiscal year);
- (ii) either: (A) has a worldwide market value of outstanding common equity (voting and non-voting) held by non-affiliates (i.e., a “public float”) of \$700 million or more, or (B) has issued in the last three years, in registered “primary offerings”²⁶ for cash (i.e., excluding exchange offers) at least \$1 billion in non-convertible securities (other than common equity); and
- (iii) is not an ineligible issuer (as discussed immediately below).

To qualify as a WKSI, an issuer must not be: a voluntary filer of Exchange Act reports²⁷ or a foreign government (as neither is eligible to use Form S-3 or F-3), a Canadian issuer filing annual reports on Form 40-F (i.e., under the MJDS), an asset-backed issuer, a registered investment company, a business development company or an “ineligible issuer” as defined in Rule 405 under the Securities Act. An “ineligible issuer” under Rule 405 includes, among others, an issuer that:

- (A) within the past three years, has filed for bankruptcy or insolvency, has been the subject of an involuntary

²⁵ Specifically, to be eligible to use Form S-3, the short form registration statement for U.S. issuers, the issuer must have timely filed all required Exchange Act reports during the 12 months and any part of a month immediately preceding the filing of the registration statement, other than current reports required solely under certain items of Form 8-K.

Form F-3, the corresponding short form registration statement for foreign private issuers, contains a similar eligibility requirement but with no exception for reports filed on Form 6-K. (Foreign private issuers use Form 6-K instead of Form 8-K.)

²⁶ A “primary offering” is an offering of securities by or for the issuer for its own account.

²⁷ See F.1.(d) below.

bankruptcy or insolvency petition²⁸ or has had a court-appointed receiver, fiscal agent or similar officer for its business or property;²⁹

- (B) has filed a registration statement that is the subject of a pending proceeding or examination under Section 8 of the Securities Act or has been the subject of a refusal or stop order under Section 8 within the past three years;
- (C) is the subject of a pending cease-and-desist proceeding under Section 8A of the Securities Act for an offering;
- (D) has been, or has a subsidiary that when it was a subsidiary of the issuer was, convicted of any felony or misdemeanor described in Section 15(b)(4)(B)(i) through (iv) of the Exchange Act during the past three years;³⁰
- (E) has been, or has a subsidiary that when it was a subsidiary of the issuer was, the subject of a judicial or administrative decree or order (including a settled claim or order) prohibiting certain conduct or activities concerning the anti-fraud provisions of the U.S. federal securities laws during the past three years; or
- (F) is or has been³¹ during the past three years a blank check company, a shell company (other than a business combination related shell company) or a penny stock issuer.

²⁸ Ineligibility based on an involuntary bankruptcy petition occurs on the earlier of: (I) 90 days after the petition is filed (if the case was not earlier dismissed), or (II) the conversion of the case to a voluntary proceeding under federal bankruptcy or state insolvency laws.

²⁹ However, such an issuer's ineligibility will end once the issuer has filed an annual report with audited financial statements after its emergence from that bankruptcy, insolvency or receivership process.

³⁰ A conviction by a foreign court as to a crime described in Section 15(b)(4)(B)(i) through (iv) of the Exchange Act would trigger ineligibility under the definition of "ineligible issuer" in Rule 405.

³¹ This includes any predecessor of the issuer.

However, the SEC may waive an issuer's ineligibility. Specifically, an issuer that would otherwise fall within the definition of ineligible issuer in Rule 405 will not be an ineligible issuer if the SEC determines, upon a showing of good cause, that it is not necessary under the circumstances that the issuer be considered an ineligible issuer. The SEC has informally stated that it intends to use this waiver ability, where appropriate, and it has done so.³² Accordingly, an issuer should consider contacting the SEC to discuss its status rather than assuming that it falls within the definition of ineligible issuer.

A majority-owned subsidiary of a WKSI is considered a WKSI under certain circumstances.

(b) Seasoned Issuer

A "seasoned issuer" is an issuer that is required to file reports under Section 13(a) or 15(d) of the Exchange Act and: (i) is eligible to use Form S-3 or F-3 to register a primary offering of securities under General Instruction I.B.1 of those Forms (i.e., has a worldwide market value of outstanding common equity held by non-affiliates (a "public float") of \$75 million or more); or (ii) is registering securities in reliance on certain instructions of Form S-3 or F-3. Under (ii) above, each of the following would be considered a "seasoned issuer": (1) an issuer registering a primary offering of non-convertible investment grade securities for cash under General Instruction I.B.2 of Form S-3 or F-3; (2) a majority-owned subsidiary registering an offering of its own securities under General Instruction I.C of Form S-3 or General Instruction I.A.5 of Form F-3; and (3) an issuer registering an offering of asset-backed securities on Form S-3. Asset-backed securities may be registered on Form S-3 if: (A) the issuer meets the requirements of General Instruction I.A.4 of Form S-3; and (B) the transaction meets the requirements of General Instruction I.B.5 of Form S-3, including that the asset-backed securities are investment grade. Additionally, an issuer that would be a WKSI except that it is an "ineligible issuer" under Rule 405 (e.g., an issuer that has engaged in certain Exchange Act violations) is considered a seasoned issuer.

(c) Unseasoned Issuer

An "unseasoned issuer" is an issuer that is required to file reports under Section 13(a) or 15(d) of the Exchange Act but is not eligible to use Form S-3 or F-3 to register a primary offering of securities under General Instruction I.B.1 of those Forms and is not registering securities in reliance on General Instruction I.B.2, I.B.5 or I.C of Form S-3 or General Instruction I.A.5 or I.B.2 of Form F-3 (e.g., an issuer that has been filing Exchange Act reports for less than one year).

Given the requirements for use of Forms S-3 and F-3, an "unseasoned issuer" will most commonly be: (i) any issuer during the 12 months after its IPO in the United States (because the issuer generally will have been filing Exchange Act reports for less than one

³² The SEC has frequently waived an issuer's status as an "ineligible issuer" under Rule 405 where the issuer has been, or has a subsidiary that when it was a subsidiary of the issuer was, the subject of a judicial or administrative decree or order (including a settled claim or order) prohibiting certain conduct or activities concerning the anti-fraud provisions of the U.S. federal securities laws during the past three years.

year); (ii) a public company that has registered only debt securities and, therefore, cannot meet the \$75 million (common equity) public float requirement of General Instruction I.B.1 of Form S-3 or F-3, including when it makes its “IPO” of equity securities; (iii) a small public company that, while having publicly registered equity, does not meet the \$75 million public float requirement of General Instruction I.B.1 of Form S-3 or F-3; or (iv) any reporting issuer³³ that has been late in a filing obligation under the Exchange Act (subject to certain exceptions) during the past 12 months or has committed one of the specified dividend or debt defaults and, therefore, has lost its eligibility to use Form S-3 or F-3 until those tests are met again. For example, a WKSI or seasoned issuer that is not timely in its Exchange Act filings and, therefore, loses its eligibility to use Form S-3 or F-3, is considered an unseasoned issuer.

(d) Non-Reporting Issuer

Issuers that are required to file reports under Section 13(a) or 15(d) of the Exchange Act (i.e., WSIs, seasoned issuers and unseasoned issuers) are collectively referred to as “reporting issuers.”

A “non-reporting issuer” is an issuer that is not required to file reports under Section 13(a) or 15(d) of the Exchange Act. Generally, a non-reporting issuer will be an issuer preparing for its IPO in the United States. A voluntary filer is also considered a non-reporting issuer. A “voluntary filer” is an issuer that is not required to file Exchange Act reports, but does so voluntarily. For example, high-yield issuers that are filing Exchange Act reports after the first year in which their registration statement on Form S-4 or F-4 under the Securities Act is effective solely to comply with covenant obligations are voluntary filers. A voluntary filer that wants to be treated as a reporting issuer should register a class of its securities under the Exchange Act.

2. Free Writing Prospectuses

(a) Overview

Rules 164 and 433 under the Securities Act allow issuers, underwriters and other offering participants (i.e., participating dealers and selling security holders) to make written offers by way of a free writing prospectus after a registration statement has been filed. But, WSIs can use a free writing prospectus even before filing a registration statement under Rule 163. Free writing prospectuses do not have to meet the extensive form and content requirements of statutory prospectuses.

(b) The Free Writing Prospectus

Section 5(b)(1) of the Securities Act makes it unlawful to transmit any “prospectus” relating to a security for which a registration statement has been filed unless the prospectus meets the requirements of Section 10 of the Act. And, Section 2(a)(10) of the Securities Act defines the term “prospectus” broadly, to include all written offers to sell a

³³ See F.1.(d) below.

security (with two exceptions). Therefore, Section 5(b)(1) generally prohibits written offers during the waiting period and post-effective period unless they are in the form of a prospectus that meets the requirements of Section 10 (i.e., a statutory prospectus). However, Rules 164 and 433 allow issuers and other offering participants to make written offers, including certain electronic communications, during an offering outside the statutory prospectus (i.e., to use “free writing prospectuses”) if certain conditions are met.³⁴

A free writing prospectus need not be in any particular form and is not required to meet the informational requirements otherwise applicable to prospectuses. A “free writing prospectus” is defined as any written communication that is an offer to sell or a solicitation of an offer to buy securities relating to a registered offering that is used after the registration statement for the offering is filed (or, for a WKSI, whether or not the registration statement is filed) other than: (i) a permitted preliminary or final statutory prospectus, or (ii) a communication delivered after effectiveness of the registration statement that is accompanied or preceded by a final prospectus (i.e., supplemental sales literature).

(i) Eligibility

A WKSI can use a free writing prospectus at any time, including before the filing of the registration statement (under Rule 163), provided that it meets the conditions outlined below (except that a free writing prospectus used under Rule 163 generally will have to be filed upon the filing of a registration statement or amendment covering the securities). Other issuers can use free writing prospectuses only after filing a registration statement. Furthermore, for an offering participant (including the issuer) to use a free writing prospectus, the issuer cannot be an “ineligible issuer” or an “excluded issuer” and the offering cannot be an “excluded offering” (each as defined below).

Ineligible issuers. For an offering participant to use a free writing prospectus (other than a free writing prospectus that consists only of descriptions of the securities in the offering or of the offering), the issuer may not be an “ineligible issuer” as defined in Rule 405 under the Securities Act (or, for an offering participant other than the issuer, the participant must have a reasonable belief that the issuer is not an “ineligible issuer” under Rule 405). The same definition is used to identify issuers ineligible to be WSIs.

“Ineligible issuers” are: (A) reporting issuers who are not current in their Exchange Act reports and other materials required to be filed during the preceding 12 months (or such shorter period that the issuer was required to file such reports and materials), other than reports required solely under certain items of Form 8-K; (B) limited partnerships offering and selling their securities other than through a firm commitment underwriting; and (C) the other issuers ineligible for WSI status under Rule 405 (as described in F.1.(a) above).

To determine whether an issuer is an “ineligible issuer” not permitted to use a free writing prospectus, the issuer’s eligibility is measured: (I) when the

³⁴ In other words, although not a statutory prospectus, a free writing prospectus that complies with Rules 164 and 433 is deemed to be a permitted Section 10(b) prospectus for purposes of Section 5(b)(1).

registration statement for the offering is filed; or (II) for an offering under a shelf registration statement, the earliest time after filing the registration statement that the issuer or another offering participant makes a bona fide offer (including by using a free writing prospectus) of the relevant securities. This timing of determination as to eligibility to use a free writing prospectus applies to all issuers (including WKSIs). The timing of determination of whether an issuer is an “ineligible issuer” for WKSI status is different and is made on an approximately annual basis.

Excluded issuers. “Excluded issuers” are defined to include: (A) registered investment companies, and (B) business development companies. These issuers cannot use free writing prospectuses.

Excluded offerings. Additionally, free writing prospectuses may not be used for these offerings: (A) business combination transactions by all issuers, and (B) offerings registered on Form S-8 by issuers other than WKSIs.

(ii) Conditions

A free writing prospectus used after the filing of the registration statement must meet the requirements of Rule 164 and the conditions of Rule 433, which include the following:

- (A) Statutory Prospectus: The use of a free writing prospectus is generally conditioned on the filing of a prospectus that meets the requirements of Section 10. A statutory prospectus must either be available or delivered to the recipient when a free writing prospectus is used. Generally, for non-reporting issuers and unseasoned issuers a statutory prospectus (including a price range if an IPO) must precede or accompany the free writing prospectus.³⁵ For seasoned issuers and well-known seasoned issuers a reference to the filing is sufficient.
- (B) Information: There is no particular information requirement for a free writing prospectus. The free writing prospectus may contain information that is not in the registration statement, but this information cannot conflict with information in the registration statement (including information in the issuer's Exchange Act reports that are incorporated by reference into the registration statement) and cannot be misleading or fraudulent.³⁶

³⁵ For an electronic free writing prospectus, including an active hyperlink to the statutory prospectus will meet this delivery requirement. Thus, a physical statutory prospectus need not be delivered if the free writing prospectus is delivered by e-mail.

³⁶ Even when filed, a free writing prospectus will not be part of a registration statement subject to liability under Section 11 of the Securities Act, unless the issuer elects to file it as part of the registration statement.

- (C) Legend: The only required content in a free writing prospectus is a legend. A free writing prospectus must include a legend: (I) indicating where a statutory prospectus is available for the offering to which the communication relates, and (II) recommending that potential investors read that prospectus (including any Exchange Act reports or other documents incorporated by reference). The legend must advise investors that they can obtain the registration statement (including the statutory prospectus and any incorporated Exchange Act documents): (I) for free on the SEC's web site, or (II) from the issuer or any underwriter or participating dealer by calling a toll-free number. The legend also must indicate that the free writing prospectus relates to a registered public offering.³⁷
- (D) Filing: As explained below, generally an issuer will have to file the free writing prospectus with the SEC no later than the day the free writing prospectus is first used. Generally, an issuer will have to file a free writing prospectus in the following circumstances: (I) where a free writing prospectus is prepared by or on behalf of the issuer or used or referred to by the issuer (i.e., where a free writing prospectus is an "issuer free writing prospectus"); (II) where a free writing prospectus prepared by or on behalf of, or used by, an offering participant other than the issuer (e.g., an underwriter) contains material information about the issuer or its securities that has been provided by or on behalf of the issuer ("issuer information") that is not already included in (or incorporated by reference into) a previously filed statutory prospectus or free writing prospectus relating to the offering (in this case, the issuer information must be filed); and (III) where a free writing prospectus (or part of it) prepared by or on behalf of the issuer or other offering participant comprises a description

However, whether or not a free writing prospectus is filed, any seller offering or selling securities by means of the free writing prospectus will be subject to potential disclosure liability under Section 12(a)(2) of the Securities Act. Additionally, a free writing prospectus can be the basis for liability under the anti-fraud provisions of the U.S. federal securities laws, such as Rule 10b-5 under the Exchange Act.

³⁷ An immaterial or unintentional failure to include the specified legend in a free writing prospectus will not preclude reliance on Rule 164 so long as: (1) a good faith and reasonable effort was made to comply with the legend condition, and (2) the free writing prospectus is amended to include or correct the legend as soon as practicable after discovery of the omitted or incorrect legend. Additionally, if the free writing prospectus has been transmitted without the correct legend, the free writing prospectus must be retransmitted with the correct legend by substantially the same means as, and directed to substantially the same prospective purchasers to whom, it was originally transmitted. For example, if the original free writing prospectus was sent by e-mail to a distribution list, the amended free writing prospectus must be e-mailed to the same distribution list.

of the final terms of the issuer's securities in the offering or of the offering (i.e., a “final term sheet”). Generally, offering participants other than the issuer (e.g., underwriters and dealers) are not required to file the free writing prospectuses that they prepare, use or refer to. This includes information prepared on the basis of or derived from, but not containing, issuer information. Such information can be, but is not limited to, information proprietary to the preparer. However, where an offering participant other than the issuer uses or refers to a free writing prospectus that is distributed by (or on behalf of) that offering participant in a manner reasonably designed to lead to its broad unrestricted dissemination, that offering participant must file the free writing prospectus with the SEC (unless it has already been filed). For example, this filing condition would apply where an underwriter: (I) includes a free writing prospectus on an unrestricted web site or hyperlinks from an unrestricted web site to information that would be a free writing prospectus, or (II) sends out a press release concerning the issuer or the offering that is a free writing prospectus. This filing condition also would apply where there was an inadvertent unrestricted distribution of a free writing prospectus prepared by an underwriter. If filing is required (whether by the issuer or another offering participant), the free writing prospectus (or part of it) generally must be filed “by a means reasonably calculated to result in filing no later than the date of first use.” However, a free writing prospectus (or part of it) that contains only a description of the final terms of the issuer's securities in the offering or of the offering must be filed by the issuer within two days after the later of: (I) the date those terms became final for all classes of the offering, or (II) the date of first use.³⁸

- (E) Record Retention: Issuers and other offering participants must retain all free writing prospectuses that they have used and not filed with the SEC, for three years following the

³⁸ An issuer or any other person may cure an immaterial or unintentional failure to file or delay in filing a free writing prospectus without losing the ability to rely on Rule 164. This cure provision is available if: (1) a good faith and reasonable effort was made to comply with the filing condition, and (2) the free writing prospectus is filed as soon as practicable after the discovery of the failure to file.

date of the initial bona fide offering of the subject securities.³⁹

3. Electronic Road Shows

A live, in-person road show to a live audience is considered an oral communication. Similarly, a live, in real-time road show presentation that is graphically transmitted to a live audience is not considered a written communication. This means that it is not considered a free writing prospectus and is simply treated like an oral offer.⁴⁰

Road shows that are recorded are deemed to be free writing prospectuses and must fulfill the conditions described above, except that electronic road shows generally are not required to be filed. However, if the issuer is a non-reporting issuer when the registration statement is filed (generally, for an issuer's IPO in the United States) and is offering common equity or convertible equity securities, this exemption from Rule 433's filing condition is available only if the issuer makes a "bona fide" version of the electronic road show available graphically to an unrestricted audience (e.g., on the issuer's unrestricted web site) no later than when the other written versions are first used. Under Rule 433, a "bona fide" version of the electronic road show is a written communication transmitted by graphic means that contains a presentation by one or more members of the issuer's management and that covers the same general areas of information concerning the issuer, such management and the securities being offered as the other written versions. Usually only one version of an electronic road show is used. For IPOs of common equity or convertible equity securities, if only one version of an electronic road show is used, that road show is subject to the filing condition of Rule 433 unless the issuer makes it available graphically to an unrestricted audience (i.e., to all potential investors).

A communication that is provided or transmitted simultaneously with a road show and is provided or transmitted in a manner designed to make the communication available only as part of the road show and not separately is deemed to be part of the road show. Therefore, if the road show is not a written communication (i.e., is an in-person road show or a live, in real-time graphically transmitted road show), such a simultaneous communication (e.g., slides or other visual aides) is also deemed not to be written (even if it would otherwise be a written communication). If the road show is written and not required to be filed, such a simultaneous communication is also not required to be filed. Otherwise, a written communication that is an offer contained in a separate file from a road show, whether or not the road show is a written communication, or otherwise transmitted separately from a road show, will be a free writing prospectus subject to any applicable filing conditions of Rule 433.

³⁹ An immaterial or unintentional failure to retain a free writing prospectus will not result in the loss of the ability to rely on Rule 164 if a good faith and reasonable effort was made to comply with the record retention condition. Whether or not there has been a good faith and reasonable effort to comply with the record retention condition will be a "facts and circumstances" determination.

⁴⁰ See E.(3)(b) above.

4. Media Publications or Broadcasts

The publicity rules address offers that take place using the media as a communication vehicle. Under the publicity rules, where an issuer or other offering participant provides issuer or offering-related information to the media, whether orally or in writing, its publication or broadcast (in any format) by the media will constitute a free writing prospectus if the written distribution of that information by the offering participant would constitute a written offer.

The treatment under Rule 433 of a media publication or broadcast that constitutes a “free writing prospectus” depends on whether the publication or broadcast was prepared or paid for by an offering participant, or whether unaffiliated media prepare and publish or broadcast the communication for no payment from an offering participant.

Where an offering participant (a) prepares, (b) pays for the preparation, publication or dissemination of, or (c) uses or refers to, a published article, television or radio broadcast or advertisement, the communication will be treated as any other free writing prospectus. For example, for offerings by unseasoned and non-reporting issuers, the publication or broadcast must be preceded or accompanied by the statutory prospectus on file with the SEC (including a price range in an IPO). Therefore, in offerings by unseasoned and non-reporting issuers, offering participants will not be able to prepare or pay for published or broadcast written advertisements, “infomercials” or broadcast spots, or similar written communications about the issuer, its securities or the offering that include information beyond what is allowed under Rule 134 (or another safe harbor) because they will not be able to ensure delivery of the statutory prospectus to all recipients of the publication or viewers of the broadcast. For offerings by seasoned issuers that are not WKSIs, a registration statement including a statutory prospectus (which can be a base prospectus) must be on file with the SEC at the time of the publication or broadcast. Additionally, the issuer or other offering participant may have to file the free writing prospectus with the SEC no later than the date of first use.

A media publication or broadcast that is prepared by unaffiliated media in which the issuer or another offering participant participates but does not pay for (i.e., an “independently prepared media publication”)⁴¹ may be a free writing prospectus.⁴² However, for independently prepared media publications that are free writing prospectuses, Rule 433(f) modifies the general conditions to use of a free writing prospectus. First, Rule 433(f) contains an exemption from the requirement for offerings by unseasoned and non-reporting issuers that a statutory prospectus

⁴¹ An “independently prepared media publication” is one for which an offering participant (or any person acting on its behalf) provided, authorized or approved information that is prepared and published or disseminated by a person that (i) is unaffiliated with any offering participant, and (ii) is in the business of publishing, radio or television broadcasting or otherwise disseminating written communications, where no payment is made by or on behalf of an offering participant for the written communication or its dissemination (i.e., for the preparation, publication or broadcast).

⁴² For example, an issuer or underwriter is permitted to invite the press to a road show, but, in most cases, the SEC will consider an article including information obtained at that road show to be a free writing prospectus of the issuer or underwriter and subject to the rules concerning free writing prospectuses.

precede or accompany the free writing prospectus.⁴³ For example, if a CEO of an unseasoned or non-reporting issuer gives an interview to a financial news magazine without payment to the magazine for the article, the publication of the article after the filing of the registration statement may be a free writing prospectus of the issuer, but need not be preceded or accompanied by a statutory prospectus. Second, Rule 433(f) provides that an independently prepared media publication that is a free writing prospectus must be filed by the issuer or other offering participant within four business days after the offering participant becomes aware of the publication, radio or television broadcast or other dissemination of the written communication. However, Rule 433(f)'s filing requirement is subject to the following: (a) in lieu of filing the actual written communication as published or disseminated, the offering participant may file a copy of the materials provided to the media, including transcripts of interviews or similar materials, provided the copy or transcripts contain all the information provided to the media; (b) the offering participant need not file the free writing prospectus if the substance of that free writing prospectus has previously been filed with the SEC; and (c) the offering participant may file, together with the free writing prospectus or afterwards, information that it reasonably believes is necessary or appropriate to correct information included in the media publication or broadcast.

An issuer that is in the business of publishing or radio or television broadcasting may rely on the special media-related rules discussed above for any publication or radio or television broadcast that is a free writing prospectus for an offering of its own securities, provided certain conditions are met.

The rules for media publications or broadcasts only apply to written offers prepared, published or disseminated by the media where the issuer or another offering participant provides, authorizes or approves the information. Media publications or broadcasts based on information filed with the SEC or otherwise publicly available are not "offers" subject to the publicity restrictions where there is no other involvement by an offering participant.

5. Web Site Information

Information on an offering participant's web site (including information hyperlinked from that web site) that is an "offer" of securities generally will be considered a free writing prospectus. Because, in an IPO, the statutory prospectus must include a price range for an offering participant to permissibly use a free writing prospectus, IPO issuers should be especially careful about their web site content.

Historical information on an issuer's web site that is not an "offer" of securities under the Securities Act will not become an offer simply because it is accessed during an offering. However, the information may become an offer if it is updated or used or referred to (by hyperlink or otherwise) by an offering participant in connection with the offering. To provide a safe harbor concerning the treatment of historical information on web sites, Rule

⁴³ While a statutory prospectus need not precede or accompany the free writing prospectus, a filed registration statement including a statutory prospectus is necessary (except for a WKSI). However, in an IPO, the filed statutory prospectus need not include a price range.

433(e)(2) provides that historical information on an issuer's web site will not be a current “offer” of the issuer's securities, even if accessed during an offering, if the information: (a) is separately identified as historical (e.g., by being dated); (b) is located in a separate section of the issuer's web site containing historical information (e.g., archives); and (c) is not incorporated by reference into or otherwise included in a prospectus of the issuer for the offering or otherwise used or referred to in connection with the offering.

Other information located on (or hyperlinked from) a web site might similarly not be considered a current “offer” of the issuer's securities and, therefore, not a free writing prospectus, where it can be demonstrated that the information was published previously. For example, certain information that, while not contained in a separate section of an issuer's web site, is dated or otherwise identified as historical information and is not referred to in connection with the offering activities may not be a current offer depending on the facts and circumstances.

G. Prospectus Delivery

1. Circulation of the Preliminary Prospectus

The SEC usually requests information about distribution of the preliminary prospectus. If the distribution is insufficient, effectiveness may be delayed. In IPOs, a preliminary prospectus must be delivered to every person who is expected to receive a confirmation of sale at least 48 hours before the confirmation is sent.

2. Recirculation of a Preliminary Prospectus

Formerly, circulation of an amended preliminary prospectus to persons who received the original preliminary prospectus (i.e., “recirculation”) was sometimes done if there was a material change to the information contained in the preliminary prospectus. Recirculation, although rare, was done to minimize potential liability and may have been required to obtain the SEC's grant of acceleration of effectiveness. Generally, issuers seek to avoid recirculation. Even before the SEC adopted securities offering reforms in 2005 (the “2005 reforms”), recirculation was not the only legal means of conveying changed information; the SEC staff often would not insist on recirculation if it received assurances that potential investors would be orally informed of material changes before being asked to commit to a purchase (i.e., before being asked to make an investment decision). As a result of the 2005 reforms, the SEC will no longer specify how material changes to the preliminary prospectus should be conveyed to potential investors. While recirculation remains one way of conveying this information, it will no longer be required. For example, certain companies may now use a free writing prospectus to convey the changes, and use of a free writing prospectus usually is preferred.⁴⁴ Nevertheless, if the changes to a circulated preliminary prospectus are extensive, the issuer and managing underwriter may prefer to print and circulate an entire revised preliminary prospectus (i.e., recirculation). As part of the 2005 reforms, the SEC adopted Rule 159 under the Securities Act. Rule 159 clarifies that, for assessing disclosure liability for prospectuses under Section 12(a)(2) of the Securities Act, information provided only after the time of sale (including the time of a contract of sale) is

⁴⁴ Such free writing prospectus must be filed with the SEC.

disregarded. The “time of sale” is when an investment decision is made; generally, this occurs shortly after pricing, when the underwriters contact their customers who have indicated an interest in purchasing securities to confirm their orders. The final prospectus is not always available by the time of sale (i.e., at or before the time of sale). Accordingly, under Rule 159, information in a final prospectus not conveyed to an investor by the time of sale is not taken into account in assessing disclosure liability under Section 12(a)(2) at the time of sale. Before the 2005 reforms were adopted, because of SEC concern that information in a final prospectus might not be communicated to investors before their investment decisions were made if, after the preliminary prospectus was widely distributed, there were material changes in disclosure, there was, as discussed above, a risk that the SEC would require recirculation or other assurances that the corrected disclosure would be provided to investors before their investment decisions were made. After the 2005 reforms were adopted, in light of Rule 159, the SEC staff has stated that it will no longer address recirculation or other issues concerning how information should be conveyed to investors before their investment decisions are made. Instead, issuers and underwriters address the disclosure liability structure provided by Rule 159 by ensuring that information is conveyed (through a prospectus, free writing prospectus or other appropriate means) by the time of a contract of sale.

3. After Effectiveness of Registration Statement

(a) Overview. Formerly, under Section 5(b) of the Securities Act, a prospectus meeting the requirements of Section 10(a) of the Act (i.e., a “final prospectus” containing all required information) had to be delivered to each investor in a registered offering with or before delivery of the confirmation of sale or the securities, whichever occurred first. Congress intended that the final prospectus provide investors with the means of understanding the intricacies of the transaction. However, the former delivery requirement did not actually protect investors because, by the time the final prospectus was received, an investment decision generally had already been made and settlement might have occurred. Additionally, the need to prepare, print and deliver final prospectuses caused extreme timing and logistical difficulties for issuers and underwriters. Last, the sanction for failing to deliver a final prospectus in accordance with the requirements of Section 5(b) was severe--the purchaser had a strict liability right to rescind the transaction under Section 12(a)(1) of the Securities Act. Accordingly, in 2005, the SEC adopted rules that generally eliminated the need to deliver final prospectuses in registered offerings. The reforms also generally eliminated the requirement that final prospectuses be delivered in the aftermarket following an offering for a specified period of time. Last, under the reforms, underwriters and dealers are allowed to send notices of allocation via e-mail.

Specifically, as part of the 2005 reforms, the SEC adopted an “access equals delivery” model for final prospectus delivery. Under an “access equals delivery” model, investors are presumed to have access to the Internet, and issuers and intermediaries can meet their delivery requirements if the filings or documents are posted on a web site. Under the final prospectus delivery reforms, that web site is the SEC’s web site. Accordingly, issuers are still required to prepare and electronically file final prospectuses with the SEC (on EDGAR). Issuers and underwriters may still choose to print final prospectuses for business-related reasons, such as for recordkeeping purposes and as a written confirmation of receipt. Further, purchasers have the right to request physical copies of the final prospectus.

(b) Statutory Scheme. During the post-effective period, Section 5(b)(2) provides that it is unlawful to use the mails or interstate commerce for the purpose of sale or delivery after sale of any security unless “accompanied or preceded” by a prospectus that meets the requirements of Section 10(a). Additionally, Rule 10b-10 generally requires a broker-dealer to deliver a written confirmation to its customer at or before completion of the transaction. Under Section 5(b)(1), after a registration statement has been filed it is unlawful to transmit a “prospectus” unless that prospectus meets the requirements of Section 10. Section 2(a)(10) defines “prospectus” to include any written communication that “confirms the sale of any security,” except that a communication sent after the registration statement’s effective date will not be considered a prospectus if before or with the communication, a final prospectus is sent to the person to whom the communication is made. Consequently, the Rule 10b-10 confirmation is a “prospectus” that does not meet the requirements of Section 10 and its transmittal would violate Section 5(b)(1) unless it is accompanied or preceded by a final prospectus. Thus, the combined result of Sections 5(b)(2) and 5(b)(1), Rule 10b-10 and the definition of “prospectus” in Section 2(a)(10) is that, absent an exemption, a final prospectus must precede or accompany the delivery of the confirmation or the security, whichever comes first.

(c) Rule 172(b): Access to the Final Prospectus Equals “Delivery” for Section 5(b)(2). Under Rule 172(b) under the Securities Act, a final prospectus will be deemed to precede or accompany a security for sale for purposes of Section 5(b)(2) as long as a prospectus meeting the requirements of Section 10(a) (i.e., a final prospectus) is filed with the SEC on EDGAR.⁴⁵ Rule 172(b) (together with Rules 172(a) and 10b-10, which are discussed below) allows settlement and delivery of securities to investors with only a written confirmation from the underwriter or dealer (which is often electronic) and no delivery of a final prospectus. Rule 172(b) covers registered offerings of securities (subject to certain exceptions)⁴⁶ as well as transactions involving unsold allotment securities and market making transactions by dealers affiliated with issuers. However, Rule 172(b) is not available if: (i) the registration statement is subject to a stop order issued under Section 8(d) or (e) of the Securities Act; or (ii) the issuer, or any underwriter or participating dealer, is subject to a cease-and-desist order for the offering under Section 8A of the Securities Act.

(d) Rule 173: Notice of Purchase in Lieu of Delivery of Final Prospectus. Rule 173 under the Securities Act provides that, for each sale of securities that requires delivery of a final prospectus, each underwriter or dealer (or, if the sale is made by the issuer, then the issuer) must send to each purchaser, no later than two business days after the sale is complete,⁴⁷ a copy of the final prospectus or, in lieu of the final prospectus, a notice providing that the sale was made under a registration statement or in a transaction in which a final prospectus would have

⁴⁵ Specifically, a final prospectus will be deemed to precede or accompany a security for sale for purposes of Section 5(b)(2) as long as the final prospectus is timely filed with the SEC or the issuer has made a good faith and reasonable effort to timely file the final prospectus (i.e., by the time required under Rule 424(b)) and, if the issuer has not timely filed it, the issuer files it as soon as practicable after discovery of the failure to file.

⁴⁶ Rule 172(b) does not apply to: (i) offerings by registered investment companies or business development companies, (ii) certain business combination transactions, or (iii) offerings registered on Form S-8.

⁴⁷ For Rule 173, the sale is complete on the date of settlement.

been required to have been delivered in the absence of Rule 172 (i.e., a “Rule 173 notice”).⁴⁸ Rule 173 also provides that if a Rule 173 notice has been sent in lieu of the final prospectus, a purchaser can request from the person responsible for sending the notice a copy of the final prospectus. However, a requested final prospectus need not be provided before settlement.⁴⁹

Compliance with Rule 173 is not a condition to reliance on the exemption from final prospectus delivery under Rule 172(b) (or Rule 172(a), which is discussed below). Therefore, non-compliance with Rule 173 will not result in a violation of Section 5 of the Securities Act. The same offerings excluded from Rule 172(b) also are excluded from Rule 173. Also excluded from Rule 173 are transactions solely between broker-dealers in reliance on Rule 153 under the Securities Act (which is discussed later).⁵⁰

(e) Rule 172(a): Written Confirmations and Notices of Allocation Without a Final Prospectus. Rule 172(a) under the Securities Act provides an exemption from Section 5(b)(1) that allows written confirmations and notices of allocation to be delivered after effectiveness even if not accompanied or preceded by a final prospectus if: (i) the information in the confirmation is limited to that called for in Rule 10b-10 and other information customarily included in written confirmations of sales; and (ii) the notice of allocation does not include information other than: (1) information identifying the securities; (2) information concerning pricing, allocation and settlement; and (3) related incidental information. This permits written communications from an offering participant to a customer or from an underwriter to dealers in the selling group notifying them of the transaction and their allocations of securities in a registered offering. For example, broker-dealers may send e-mail notices after effectiveness informing investors in a public offering of their allocations.

The availability of the Rule 172(a) exemption is conditioned on the final prospectus being filed with the SEC.⁵¹ The Rule 172(a) exemption is not available if: (i) the registration statement is subject to a stop order issued under Section 8(d) or (e); or (ii) the issuer, or any underwriter or participating dealer, is subject to a cease-and-desist order for the offering under Section 8A. Additionally, the Rule 172(a) exemption is not available for the same offerings excluded from Rule 172(b).

⁴⁸ The Rule 173 notice can be sent separately or can be included in a Rule 10b-10 confirmation.

⁴⁹ Additionally, Rule 15c2-8(d) under the Exchange Act requires underwriters and selling group members to take reasonable steps to promptly send final prospectuses to all those who make written requests for one between the effective date of the registration statement and the later of: (i) the termination of the distribution, or (ii) the expiration of 40 days after the first date that the security was bona fide offered to the public. The 40-day period in (ii) above is extended to 90 days for an issuer’s IPO in the United States.

⁵⁰ While Rule 173 does not apply to transactions between broker-dealers in reliance on Rule 153, it does apply to the transaction between the broker-dealer and the underlying purchaser on whose behalf or for whose account the transaction is effected.

⁵¹ Specifically, the exemption is available as long as the final prospectus is timely filed with the SEC or the issuer has made a good faith and reasonable effort to timely file the final prospectus and, if the issuer has not timely filed it, the issuer files it as soon as practicable after discovery of the failure to file.

(f) Section 4(3) and Rule 174: Dealers' Exemption From Aftermarket Prospectus Delivery. Transactions by the issuer or an underwriter are subject to the prospectus delivery requirements of Section 5(b) whenever the transactions occur. Additionally, unless SEC rules provide otherwise, all dealers must deliver final prospectuses in secondary market transactions for a specified period of time after the registration statement becomes effective. Section 4(3) of the Securities Act exempts from the prospectus delivery requirements of Section 5 transactions by a dealer (including an underwriter no longer acting as such) in securities not constituting part of an unsold allotment, if the transaction has not occurred before the expiration of 40 days after the registration statement's effective date or the first date that the security was bona fide offered to the public, whichever is later (any time during which a stop order issued under Section 8 is in effect as to the security must be excluded in computing the 40-day period). The 40-day period is extended by the statute to 90 days for an issuer's IPO in the United States.

Section 4(3) authorizes the SEC to shorten the statutory periods, which it has done via Rule 174 under the Securities Act. For dealers (including underwriters and selling group members no longer acting as such in the security involved in the transactions), Rule 174 provides that: (i) no prospectus delivery is required where the registration statement of a foreign private issuer using American Depositary Receipts is on Form F-6 (provided the underlying deposited securities need not be registered under the Securities Act);⁵² (ii) no prospectus delivery is required where the issuer was a reporting issuer immediately before the filing of the registration statement; (iii) where the issuer was not a reporting issuer immediately before the filing of the registration statement (generally, for an issuer's IPO in the United States), final prospectuses must be delivered for 25 days after the offering date⁵³ if, as of the offering date, the security is listed on a registered national securities exchange (including NASDAQ); (iv) where the offering is by a blank check company, final prospectuses must be delivered until 90 days after the date funds and securities are released from the escrow or trust account under Rule 419 under the Securities Act; and (v) for a shelf registration statement, no new prospectus delivery period applies for dealers trading after the expiration of the initial 40 or 90-day period following the first bona fide offering of securities off the shelf.

Rule 174 retains the overriding obligation that a dealer deliver a prospectus when acting as an underwriter or disposing of an allotment, as well as the statutory exclusion for the period of a stop order when computing the prospectus delivery period.

As part of the 2005 reforms, the SEC amended Rule 174 to eliminate any dealer requirement to physically deliver a final prospectus under Section 4(3) and Rule 174 if a final prospectus has been posted on EDGAR and Rule 172 is otherwise complied with (except for offerings by blank check companies). Nevertheless, dealers making aftermarket sales within the prospectus delivery period of Section 4(3) and Rule 174 must send a Rule 173 notice to purchasers no later than two business days after the sale is complete (i.e., Rule 173 applies where Section 4(3) requires prospectus delivery and where there is no exemption from delivery under Rule 174).

⁵² Form F-6 is discussed in the next chapter.

⁵³ For this purpose, the "offering date" is the later of the registration statement's effective date or the first date that the security was bona fide offered to the public.

(g) Rule 153: Transactions on an Exchange or Through a Registered Trading Facility. Under Rule 153, broker-dealers effecting transactions on or through a registered national securities exchange or trading facility thereof, through a trading facility of a registered national securities association, or through a registered alternative trading system will be deemed to meet their final prospectus delivery obligations under Section 5(b)(2) between each other if: (i) the issuer has filed, or will file, the final prospectus with the SEC; (ii) securities of the same class as the securities that are the subject of the transaction are trading on that exchange or through that trading facility or alternative trading system; (iii) the registration statement is effective and not subject to a stop order issued under Section 8(d) or (e); and (iv) neither the issuer nor any underwriter or participating dealer is subject to a cease-and-desist order for the offering under Section 8A.

Rule 153 does not affect final prospectus delivery obligations to purchasers other than broker-dealers.

H. The Underwriting Process

1. The Underwriting Agreement (and Other Underwriting Documents)

Besides the registration statement (and the indenture, for a debt offering), the basic documents governing underwritten offerings of securities in the United States are: (a) the underwriting agreement (often called the "purchase agreement"), in which the underwriters commit to purchase the securities from the issuer or selling security holders; (b) the agreement among underwriters, which establishes the relationship among the managing underwriter, any co-managers and the other members of the underwriting syndicate and governs the mechanics of the distribution; and (c) the selected dealers agreement, in which dealers that are not members of the underwriting syndicate (called the "selling group") agree to certain provisions concerning the distribution. (Although each member of the underwriting syndicate agrees to underwrite a specific percentage of the total amount of the securities offered, the managing underwriter determines the allotments to the selling group dealers who rapidly sell the securities to the public. The managing underwriter, members of the underwriting syndicate and selected dealers each receive part of the underwriting spread for their efforts.) The underwriting documents generally are prepared in preliminary form by underwriters' counsel. While each of the major U.S. investment banks has its own underwriting documents, the documents used by the various firms are basically similar. Additionally, most firms have a master agreement among underwriters that applies to all offerings for which they will act as managing underwriter and is pre-signed by the firms expected to participate in their deals.

Generally, the only binding agreement between the issuer (or the selling security holders) and the underwriting group is the "underwriting agreement" which is signed by the managing underwriter(s) on behalf of the underwriting group. Although it sets forth the rights and obligations of the issuer and the underwriters (including the underwriters' obligation to purchase the securities), it is subject to various conditions and escape clauses, commonly called "outs." The underwriting agreement generally describes the securities offered, the type of

transaction (primary, secondary or both),⁵⁴ the size and price of the offering, the over-allotment option (if any),⁵⁵ the type of underwriting arrangement (e.g., firm commitment), various closing matters, the agreements and covenants of the issuer and the conditions precedent to the underwriters' obligation to purchase the securities at the closing (e.g., delivery of: officers' certificates, comfort letters from the issuer's independent public accountants and legal opinions from issuer's and underwriters' counsel (and selling security holders' counsel, if any)). It also contains: representations and warranties of the issuer (concerning, among other matters, the material accuracy of the registration statement and prospectus, the absence of any stop order suspending the use of any prospectus, the issuer's legal status and financial condition, the status of legal proceedings concerning the issuer and the absence of conduct by the issuer, or its officers, directors or affiliates, that could be deemed to constitute stabilization or manipulation of the price of the securities); indemnification and contribution provisions; termination provisions (sometimes called "force majeure" clauses); and other terms concerning the relationship between the issuer or the selling security holders and the underwriters (e.g., provisions concerning the arm's length commercial nature of the relationship between the issuer or selling security holders and the underwriters and provisions concerning default by one or more of the underwriters).

In turn, the managing underwriter enters into an agreement, called the "agreement among underwriters," with the other underwriters in the syndicate. The agreement among underwriters gives the managing underwriter the authority to negotiate the terms of, and execute, the underwriting agreement on behalf of the participating underwriters as well as broad authority to manage the distribution. The agreement among underwriters permits the managing underwriter to, among other things: determine the amount of securities to be available to each underwriter and selected dealer for direct retail sale; exercise any over-allotment option; effect stabilizing bids and purchases for the account of the underwriting syndicate;⁵⁶ require individual underwriters to deliver to it unsold securities (at the public offering price less an amount not greater than the selling concession)⁵⁷ for the purpose of reducing the syndicate short position;⁵⁸ and arrange loans and pledge securities on behalf of the underwriters or advance its own funds (and charge interest). The agreement among underwriters also contains: trading restrictions, a penalty clause,⁵⁹ the components of the underwriting spread (e.g., the management fee and

⁵⁴ As discussed earlier, "primary offerings" are offerings of securities by or for the issuer for its own account. "Secondary offerings" are offerings of securities by shareholders.

⁵⁵ See H.3. below.

⁵⁶ During equity offerings the managing underwriter is authorized to stabilize the market on behalf of the underwriting syndicate. Typically, the managing underwriter does this by placing a bid for the security being underwritten at a price at, or just below, the public offering price. Stabilizing bids and purchases are intended to peg or put a floor under the market to prevent the overhanging supply of securities that are being distributed from depressing the market during the distribution.

⁵⁷ The "selling concession" is the amount paid to the underwriter (or selected dealer) for actually selling the securities.

⁵⁸ A "syndicate short position" is created when the managing underwriter accepts orders for more securities than are to be sold (i.e., over-allots for the account of the syndicate).

⁵⁹ A syndicate bid under the penalty clause of the agreement among underwriters is known as a "penalty bid." The penalty clause (also called the "penalty bid provision") allows the managing underwriter to reclaim a selling concession paid to a syndicate member if that syndicate member's customers sell their allocated shares in the

selling concession), payment and delivery terms and obligations of the underwriters to increase their commitments if one or more of the underwriters defaults. The agreement also includes various provisions concerning the settlement of claims, exculpation, indemnification and termination, as well as representations of the participating underwriters (concerning such matters as: selling the securities at the specified public offering price, familiarity with the prospectus delivery requirements of the federal securities laws, compliance with certain requirements of the Financial Industry Regulatory Authority, Inc. ("FINRA") and, if applicable, Federal Reserve Regulation K, use of free writing prospectuses, use of "electronic underwriting" procedures (with the consent of the managing underwriter) and the approval of those procedures by the SEC and compliance with Rule 15c3-1 under the Exchange Act (the "net capital rule")).

The final basic underwriting document is the selected dealers agreement, also called the "selling agreement." This agreement is entered into between the managing underwriter (on behalf of the syndicate) and selected dealers (also called "selling group dealers") after the registration statement has been declared effective.⁶⁰ Because the underwriters may not be able to find purchasers for all of the securities, they enter into such an agreement with selected dealers to stimulate broad interest in the securities offered and to promote a rapid sale of the offering. If a rapid sale of the offering were not to occur, the issue might become sticky, depressing the sales price of the securities and reducing or eliminating the underwriters' profit.

In the selected dealers agreement, the selected dealers agree to purchase from the syndicate (at the public offering price less a specified concession) part of the securities being offered and to sell those securities at the public offering price (except in sales to other selected dealers, which are made at the public offering price less part of that concession). In the agreement, the dealers make the same representations as the underwriters concerning FINRA compliance and familiarity with the prospectus delivery requirements of the federal securities laws. Selected dealers agreements typically contain: (a) in an IPO, a penalty clause (requiring repayment of the selling concession if the syndicate purchases in the open market securities sold by the dealer); and (b) other routine provisions concerning the distribution (e.g., to the extent the dealer has unsold shares, the managing underwriter retains the right to repurchase those shares, at not less than the selected dealer's cost, so that the syndicate can meet its obligations to purchasers).

immediate aftermarket. Penalty bids are assessed at the election of the managing underwriter, and are not assessed in all offerings. Indeed, penalty bids are rarely assessed. They are assessed most often in offerings for which there is relatively low demand to help prevent triggering or exacerbating a market price decline through investor sales of IPO shares. Managing underwriters justify the use of penalty bids by claiming that, if the securities are sold within a short period of time (i.e., "flipped"), the syndicate member has not earned its commission (i.e., has not sold the shares to long-term investors) and, therefore, the syndicate is entitled to reclaim the associated selling concessions through the penalty bid provision.

⁶⁰ Where a master selected dealers agreement is used, dealers that participate in offerings managed by a particular underwriter sign the master selected dealers agreement which governs all future underwritings managed by that underwriter. The practice of requiring dealers to enter into selling agreements for specific transactions has basically disappeared because the major investment banking firms have adopted master selling agreements.

2. Procedure

After the registration statement is publicly filed with the SEC (but before it is declared effective), the underwriting group "pre-sells" (i.e., obtains "indications of interest" for) the offering. As discussed earlier, this process is commonly referred to as "bookbuilding."

At the end of the bookbuilding period, which may last from a few days to a few weeks, the managing underwriter negotiates the price of the securities and the size of the offering with the issuer (or the selling security holders) based on the indications of interest and other relevant factors. In a public offering of shares that are already listed on a securities exchange, the share price usually is based on the quoted share price or a formula related to that price.

If the offering appears presold when the registration statement is ready to be declared effective, pricing may be done before effectiveness (i.e., first, the offering price and related matters are agreed upon,⁶¹ then the agreement among underwriters (if a master agreement among underwriters is not in effect) and the underwriting agreement are signed, the pricing amendment to the registration statement is filed with the SEC,⁶² the registration statement is declared effective,⁶³ and last, the underwriters begin selling the securities).

Alternatively, pricing may be done after effectiveness if Rule 430A procedures are used. Under this alternative, first, the pre-effective amendment to the registration statement is filed with the SEC (omitting price information and information about the composition of the underwriting syndicate). Then the registration statement is declared effective. After effectiveness, the offering price and related matters are agreed upon, the agreement among underwriters and the underwriting agreement are signed, and finally, the underwriters begin selling the securities.

Where securities of a foreign issuer will be listed on a U.S. exchange the securities may be priced so that they trade first on the U.S. exchange (at the opening of business) or so that they trade first on the primary exchange outside the United States (where there will be greater liquidity). In either case, pricing the offering after the registration statement has been declared effective provides the most flexibility. Accordingly, pricing usually is done after effectiveness. Assuming that is the case, as soon as possible after pricing, relevant pricing terms

⁶¹ The price will be set after the close of the market on the day before the registration statement is to be declared effective.

⁶² The pricing amendment is an amendment to the registration statement filed shortly before effectiveness that contains final corrections and changes and information not previously known, such as the public offering price, other price-related information and the names of the underwriters.

⁶³ Assuming that all SEC comments have already been addressed (as is almost always the case), the SEC will declare the registration statement effective immediately after the pricing amendment is filed. Specifically: (a) it is customary for the underwriting agreement to be signed only after notice of SEC clearance or non-review is received; (b) the pricing amendment is then filed and the issuer and managing underwriter request that it be accelerated so that the registration statement will become effective typically within an hour or two; and (c) the SEC ordinarily grants such acceleration requests.

and any other material changes are conveyed to investors, usually orally for equity securities or through a term sheet for debt securities, the form of which usually has been agreed in advance between the issuer and the underwriters.⁶⁴ The underwriters generally confirm their sales orally, followed by a written confirmation of sale that is required by Rule 10b-10 to include specific information. A final prospectus containing the offering price and other information omitted when the registration statement became effective (i.e., containing the Rule 430A information) is filed with the SEC under Rule 424(b) within 15 business days after the effective date but in no event later than the second business day after the earlier of the day the offering is priced or the day the prospectus containing the Rule 430A information is first used (i.e., available to the managing underwriter, syndicate members or offerees).

3. The Over-Allotment Option

The "over-allotment option" is the underwriters' option to purchase additional securities from the issuer. In firm commitment offerings, underwriters often obtain an over-allotment option that enables them to purchase from the issuer (or the selling security holders) up to an additional 15% of the securities being offered. The option can be exercised during a specified period (usually, within 30 days after the effective date), and can be exercised only at the original public offering price less the underwriting discount. The term "over-allotment option" implies that the option can be used only to cover over-allotments (i.e., short sales) to customers, and both underwriting agreements and prospectuses frequently describe the option as being intended for that purpose. However, in several recent offerings, the option was not so limited. Consistently, some firms provide in their master agreement among underwriters that they may elect in a given offering that the option will not be limited to that purpose. Basically, the over-allotment option is a risk control device for the underwriters.

I. Closing

At the closing, the issuer usually receives the public offering price less the agreed upon underwriters' compensation. Unless the issuer and managing underwriter agree otherwise, in a registered firm commitment underwriting for cash, the closing must take place within three business days after the underwriting agreement is entered into (or, within four business days, provided the offering is priced after 4:30 p.m. Eastern time). This gives the underwriters time to collect funds from their customers.⁶⁵ As discussed earlier, the closing is subject to certain conditions being met, including the delivery of legal opinions and accountants' comfort letters,

⁶⁴ Where a pricing term sheet is used, it is filed with the SEC under Rule 433 within two days after the later of: (a) the date the final terms have been established, or (b) the date of first use.

⁶⁵ Rule 15c6-1 under the Exchange Act instituted a three-day settlement cycle for most securities trades involving U.S. broker-dealers. Four-day settlement is prescribed by Rule 15c6-1 in the case of sales for cash of securities sold by an issuer to an underwriter on a firm commitment basis in an offering registered under the Securities Act, or sold to an initial purchaser by a broker-dealer participating in such an offering, if the offering is priced after 4:30 p.m. Eastern time. (Before Rule 15c6-1 was adopted, a five-day period between the signing of the underwriting agreement and the purchase of the underwritten securities was standard in U.S. offerings.)

While in U.S. offerings by U.S. issuers, the closing typically occurs three or four business days after the signing of the underwriting agreement, in U.S. offerings by foreign issuers, the closing sometimes does not occur until five or more business days after the signing of the underwriting agreement.

the absence of material adverse changes in the issuer's business and the absence of serious disruptions in the financial markets.

If the over-allotment option is exercised after the closing, another closing will be held for the additional shares. Moreover, if the over-allotment option is exercised and settled after the closing of the offering of the underwritten (i.e., firm) shares, the issuer generally is expected to bring down (i.e., extend) its representations, warranties and officers' certificates to the time of the over-allotment closing. However, "10b-5 opinions" concerning the absence of material misstatements or omissions in the offering materials, and accountants' comfort letters concerning the financial information contained in the offering materials, sometimes are not required.

In a best efforts underwriting, the closing takes place after the minimum or entire distribution is completed provided the distribution is completed within a specified time period (usually 60, 90 or 120 days).

J. FINRA Review

The Financial Industry Regulatory Authority, Inc. ("FINRA"), as successor to the NASD, reviews the underwriting arrangements to make sure that the underwriters' compensation is not excessive under FINRA rules. The SEC will not declare a registration statement effective until it has received the FINRA opinion that the underwriters' compensation is not excessive.

K. Blue Sky Laws

Each state has adopted its own laws regulating the offer and sale of securities within that state, called "blue sky" laws. Although there are many similarities, the laws do vary in important respects from state to state. Generally, state blue sky laws require registration or qualification of securities offered and sold to persons in that state, unless an exemption is available. Thus, an offering of securities in the United States must be registered not only with the SEC, but also with each state in which the securities will be offered (unless exempt under state law or state registration is preempted by federal law). Accordingly, when securities are offered and sold in the United States, the blue sky laws of the relevant states must be reviewed.⁶⁶

L. Merit Statutes

Unlike the Securities Act, many state statutes are "merit statutes," i.e., the state securities commissioner may prohibit the sale of a security if he determines that the sale would not be fair, just or equitable to residents of his state.

M. Listing Exemption

Offerings of securities to be listed on specified exchanges or tiers thereof (e.g., the NYSE, the NYSE Amex, Tier I of NYSE Arca, or NASDAQ (all 3 tiers)) are preempted from

⁶⁶ Additionally, when a secondary trading market develops in the United States, it is necessary to verify that exemptions exist under the blue sky laws of the various states to permit secondary trades of the securities (unless the blue sky laws concerning secondary trading are preempted by federal law).

registration or qualification, review or imposition of conditions on offering materials, and prohibitions or conditions based on the merits of the offering or issuer, by any state.

N. Shelf Registration

1. Introduction

Shelf registration enables issuers to access the U.S. capital markets in one or more offerings on demand without obtaining additional SEC approval until all the securities registered have been sold. The shelf registration rule, Rule 415 under the Securities Act, permits the registration of continuous or delayed securities offerings in the future, called "shelf registration." The securities so registered can be sold in a single offering or in an unlimited number of separate offerings until all the securities registered have been sold.

Rule 415 is a procedural rule. It applies to securities that are registered on any form of registration statement and that are intended to be offered on a delayed or continuous basis. It does not affect the eligibility of an issuer to use a particular form, nor does it change any of the disclosure requirements of the form, except that it may add items.

Shelf registration was developed to permit certain widely followed companies to register their securities without a specific transaction in mind, so that they could later offer those securities quickly without further SEC action.

2. Advantages of Shelf Registration

Shelf registration provides significant benefits for issuers by reducing costs compared to conventional securities registration procedures. First, the procedural flexibility provided by shelf registration enables an issuer to time its offering to more quickly take advantage of favorable market opportunities and, thereby, lower its financing costs. For example, an issuer can: (a) time its offering to obtain lower interest rates on debt or lower dividend rates on preferred stock in a volatile market, (b) vary the structure and terms of the securities on short notice to meet the demands of the marketplace, (c) design new issues more easily, and (d) choose quickly among alternative distribution techniques. Second, increased competition among underwriters to distribute primary offerings has reduced financing costs through lower underwriting spreads and offering yields. Third, simpler and more flexible securities registration procedures have also led to lower issuance costs. Expenses (such as legal, accounting, printing and related expenses) have been reduced as a result of only one registration statement being filed for a series of offerings. An offering off the shelf does not require the drafting of whole new offering documents or agreements. Issuers complete their securities registration before any planned sales⁶⁷ and, thereafter, periodically sell the securities, in one or more offerings, without further SEC clearance. When the terms of each offering are agreed upon, a brief prospectus supplement is prepared containing the price, description of securities and plan of distribution, together with disclosure of any material recent events not previously

⁶⁷ But see N.4.(a) below (discussing immediate shelf takedowns).

disclosed.⁶⁸ The underwriting agreement is then signed and sales are made immediately and confirmed to investors. Last, another benefit of shelf registration is that, for debt securities or guarantees, the indenture is already in place when the offering begins, which facilitates a quick closing.

3. Disadvantages of Shelf Registration

There are certain disadvantages to the use of shelf registration. For shelf offerings, Rule 415 reduces the ability of underwriters to conduct an effective due diligence review of the registration statement. The fast time schedules for shelf offerings, increased competition among underwriters and incorporation of documents by reference under the integrated disclosure system have resulted in a qualitative loss in the ability of underwriters to conduct due diligence investigations. The fast time schedules and lowered fees for shelf offerings do not permit traditional due diligence investigations. The shelf registration statement is typically prepared by the issuer's counsel and incorporates Exchange Act reports by reference, often without participation by the underwriter. And, underwriters may not have the opportunity to independently review Exchange Act documents prepared by the issuer and incorporated by reference. Shelf registration also has undermined the stability of long-term traditional relationships between underwriter and issuer. Since the adoption of Rule 415, underwriters have been selected competitively on a transaction basis in an effort by issuers to lower their financing costs, and issuers in effect have sacrificed long-term relationships with one underwriter and the expert advice they received based on that relationship. Some issuers using the shelf registration process chose one law firm to serve as "designated underwriters' counsel" for all offerings to be made from the shelf facility. This arrangement enables underwriters' counsel to review and participate in the filing of the registration statement and to conduct due diligence over the life of the shelf facility. Although this practice generally results in the review of all important documents and gives the underwriters some degree of comfort, it does not solve every due diligence problem. However, the typical shelf offering has been a debt offering by an issuer that qualifies for short form registration. That, together with Exchange Act reporting, presents less risk to investors and some sacrifice in due diligence standards has been accepted.⁶⁹

4. Shelf Registration Rule: Rule 415

Shelf registration is governed by Rule 415 under the Securities Act. The following is a description of Rule 415.

⁶⁸ Except for disclosure in the prospectus supplement of material recent developments not previously disclosed in an Exchange Act filing, the description of the issuer (and of any guarantor) will have been completed before the offering and will be included in the base prospectus, and the registration statement containing the base prospectus will have been declared effective.

For foreign private issuers, Item 8 of Form 20-F requires that financial statements not be older than a specified period before the commencement of an offering. Thus, Item 8 imposes certain limits on when offers may be made off the shelves of foreign private issuers.

⁶⁹ But see *In re WorldCom, Inc. Sec. Litig.*, 346 F. Supp. 2d 628, Fed. Sec. L. Rep. (CCH) ¶ 93,057, Fed. Sec. L. Rep. (CCH) ¶ 93,062 (S.D.N.Y., Dec. 15, 2004) (No. 02 Civ. 3288 (DLC)) (holding that underwriters have the same due diligence obligations for a shelf offering as for a non-shelf offering).

(a) Eligible Transactions

Rule 415 provides that securities may be registered for an offering to be made on a continuous or delayed basis in the future in one of eleven categories of offerings. Unless the transaction or securities fall within one of the first nine categories, they must qualify under the tenth, which means the transaction must be a primary offering of securities by a short form (Form S-3 or F-3) qualified issuer. Otherwise, the securities may not be registered for delayed or continuous offerings. The eleventh category relates to certain closed-end investment companies and business development companies. Specifically, the transactions and securities eligible for shelf registration under Rule 415 are:

1. securities to be offered or sold solely by or on behalf of a person other than the issuer, a subsidiary of the issuer or a person of which the issuer is a subsidiary (i.e., secondary offerings) (Rule 415(a)(1)(i) or shelf category (i));
2. securities to be offered and sold under a dividend or interest reinvestment plan or an employee benefit plan of the issuer (Rule 415(a)(1)(ii) or shelf category (ii));
3. securities to be issued upon the exercise of outstanding options, warrants or rights (Rule 415(a)(1)(iii) or shelf category (iii));
4. securities to be issued upon the conversion of other outstanding securities (Rule 415(a)(1)(iv) or shelf category (iv));
5. securities pledged as collateral (Rule 415(a)(1)(v) or shelf category (v));
6. securities registered on Form F-6 (i.e., American Depositary Receipts) (Rule 415(a)(1)(vi) or shelf category (vi));
7. mortgage related securities, including mortgage backed debt and mortgage participation or pass through certificates (Rule 415(a)(1)(vii) or shelf category (vii));
8. securities to be issued in connection with business combination transactions (Rule 415(a)(1)(viii) or shelf category (viii));
9. securities the offering of which will begin promptly, will be made continuously, and may continue for more than 30 days from the date of initial effectiveness (Rule 415(a)(1)(ix) or shelf category (ix));⁷⁰

⁷⁰ Examples of shelf offerings within this category are: (a) exchange, rights, subscription and rescission offers; (b) offers to employees, consultants or independent agents; (c) best efforts offerings; (d) tax shelter and other limited partnership interests; (e) commodity funds; (f) condominium rental pools; and (g) real estate investment trusts.

10. securities registered (or qualified to be registered) on Form S-3 or F-3 that are to be offered and sold on an immediate, continuous or delayed basis by or on behalf of the issuer, a majority-owned subsidiary of the issuer or a person of which the issuer is a majority-owned subsidiary (Rule 415(a)(1)(x) or shelf category (x));⁷¹ and

11. shares of common stock to be offered and sold on a delayed or continuous basis by or on behalf of a registered closed-end management investment company or business development company that makes periodic repurchase offers under Rule 23c-3 under the Investment Company Act (Rule 415(a)(1)(xi) or shelf category (xi)).

The shelf category most used is shelf category (x) (i.e., primary offerings on Form S-3 or F-3). Because the SEC expanded eligibility for short form registration for foreign private issuers and made the unallocated shelf registration process (discussed below) available to them as well, more foreign private issuers will be allowed the increased financing flexibility and efficiency that U.S. issuers enjoy under Rule 415(a)(1)(x) shelf registration. The unallocated shelf registration process allows issuers eligible to register primary offerings on Form S-3 or F-3 to use one registration statement to register an aggregate dollar amount of securities to be offered and the classes to be covered, such as debt, equity and other securities, without specifying a dollar amount for each class of securities to be offered. In this “unallocated,” or “universal,” shelf registration, the registration statement lists the types of securities covered and the prospectus supplement for an offering specifies the amount of each particular class of securities being offered up to the total dollar amount of securities registered. The value of each offering is subtracted from the total dollar amount of securities registered.

Rule 415 is not available where the registration statement relates to securities issued by a face-amount certificate company or redeemable securities issued by an open-end management company or unit investment trust under the Investment Company Act. Additionally, Rule 415 is not available for a registration statement filed by any foreign government or its political subdivisions. However, seasoned foreign governments (including

⁷¹ Formerly, issuers that filed shelf registration statements for a continuous or delayed offering on Form S-3 or F-3 could not make an immediate takedown off the shelf after it was declared effective unless the takedown was disclosed in the shelf registration statement. However, the SEC has amended Rule 415 to allow primary offerings on Form S-3 or F-3 to occur immediately after effectiveness of a shelf registration statement.

As part of the 2005 reforms, the SEC adopted Rule 430B under the Securities Act. Rule 430B is a shelf offering corollary to Rule 430A in that it describes the type of information that primary shelf eligible issuers (i.e., issuers eligible to use Form S-3 or F-3 for primary offerings) and automatic shelf issuers may omit from a base prospectus in a Rule 415 offering and include instead in a prospectus supplement, an Exchange Act report incorporated by reference or a post-effective amendment. As part of the 2005 reforms, the SEC amended Rule 415(a)(1)(x) to allow primary offerings on Form S-3 or F-3 to occur immediately after effectiveness of a shelf registration statement. For immediate offerings from an effective shelf registration statement, the SEC’s former rules permitted omission of information from the prospectus at the time of effectiveness only in reliance on Rule 430A. However, the SEC believed the changes it was adopting affecting the treatment of prospectus supplements provided sufficient protection to investors to allow, in an immediate offering, omission of information under Rule 415 and Rule 430B. Rule 430A continues to be available for immediate takedowns where the prospectus contained in the registration statement at the time of effectiveness omits only Rule 430A information. As part of the 2005 reforms, the SEC amended Rule 430A to enable the Rule to be relied on by issuers using automatic shelf registration statements.

their political subdivisions) have been permitted by the SEC to use a shelf registration procedure substantially similar to Rule 415.

(b) Additional Conditions

There are additional conditions to an effective shelf registration under Rule 415. The following is a description of those conditions.

(i) Duration of the Registration Statement

Formerly, securities registered in shelf categories (viii) (business combinations), (ix) (continuous offerings for more than 30 days after effectiveness) and (x) (standard Form S-3 or F-3 primary issuances) could only be registered in an amount that, at the time the registration statement became effective, was reasonably expected to be offered and sold within two years from the initial effective date of the registration statement. As a result of the 2005 reforms, the two year limitation no longer applies to shelf offerings in category (x) and only applies to: (a) shelf offerings in category (viii) (business combinations), and (b) shelf offerings in category (ix) (continuous offerings) that are not registered on Form S-3 or F-3.

Under the current rules, securities registered on an automatic shelf registration statement or securities described in shelf categories (vii) (mortgage-related securities), (ix) (continuous offerings) and (x) (standard Form S-3 or F-3 primary issuances) may be offered and sold for three years after the initial effective date of the registration statement. There is no limit on the amount that can be registered. Unused amounts can be carried forward.

Under the current rules, new shelf registration statements must be filed every three years for an automatic shelf registration statement or offerings under shelf categories (vii), (ix) and (x). The new registration statement and prospectus must include all the information that would then be required in a prospectus relating to all offerings that it covers. As a result, new shelf registration statements will need to be filed every three years, with unsold securities and unused fees carried forward to the new registration statement. If the new registration statement is not an automatic shelf registration statement, so long as the new registration statement is filed within three years of the original effective date of the old registration statement, offers and sales of securities from the old registration statement may be made up to six months after the filing of the new registration statement, but before its effectiveness, to allow issuers time to file and go effective under a new registration statement. Additionally, a continuous offering of securities covered by the prior registration statement that commenced within three years of the initial effective date may continue until the effective date of the new registration statement if the offering is permitted under the new registration statement. If the new registration statement is an automatic shelf registration statement, it will be effective immediately upon filing with the SEC (under Rule 462(e) under the Securities Act). Consequently, there is no six-month extension for automatic shelf registration statements.

(ii) At-The-Market Offerings

Currently (i.e., as a result of the 2005 reforms), an “at-the-market offering” is “an offering of equity securities into an existing trading market for outstanding shares of the same class at other than a fixed price.” Currently, the only limitation on an at-the-

market offering is that it must be made under shelf category (x).

(iii) Issuer Undertakings

For Rule 415 to be available, the issuer must provide the undertakings required by Item 512(a) of Regulation S-K.

As part of the reforms adopted in 2005, the SEC revised the issuer undertakings that are required for a shelf registration statement.

Before the 2005 reforms were adopted, Item 512(a)(1) required an issuer that had registered securities under Rule 415 to undertake to file a post-effective amendment to the registration statement to:

- include in the registration statement any prospectus required by Section 10(a)(3) of the Securities Act;
- reflect in a prospectus included in the registration statement any facts or events arising after the effective date of the registration statement (or the most recent post-effective amendment to it) that, individually or in the aggregate, represented a fundamental change in the information set forth in the registration statement; and
- include in a prospectus included in the registration statement any material information concerning the plan of distribution not previously disclosed in the registration statement or any material change to such information in the registration statement.

Formerly, shelf issuers could satisfy the first two of these obligations by filing Exchange Act reports that were incorporated by reference into the registration statement. As part of the 2005 reforms, the SEC amended Item 512(a)(1) to provide that, in shelf registration statements filed on Form S-3 or F-3, all of the disclosures required by this undertaking may be made in any filed prospectus supplement or any Exchange Act report incorporated by reference into the registration statement, including through an incorporated Form 8-K or 6-K. This eliminates the requirement for a post-effective amendment under such circumstances for shelf registration statements filed on Form S-3 or F-3.

As part of the 2005 reforms, the SEC amended Forms S-3 and F-3 to allow any information required in the base prospectus under Items 3 through 11 of Form S-3 and under Items 3 through 5 of Form F-3 to be incorporated by reference from filed Exchange Act reports. This includes risk factors, ratio of earnings to fixed charges, use of proceeds, determination of offering price, dilution, selling security holders, plan of distribution, description of securities, interests of named experts and counsel and material changes. Therefore, all of this information can be included in Exchange Act reports or in the prospectus or a prospectus supplement (which would be deemed part of the registration statement).

If satisfaction of any element of the undertaking requires the filing by any of the permitted methods of a consent of an expert, that consent may be filed by post-effective amendment to Part II of the registration statement or by filing of an Exchange Act report, such as an annual report on Form 10-K or 20-F or a report on Form 8-K or 6-K, that is incorporated by reference into the registration statement.

However, the SEC did not modify Item 512(a)(4), under which foreign private issuers are required to include an undertaking concerning the updating of the financial and other information in a shelf prospectus in accordance with the age of financial statements provisions under Item 8.A of Form 20-F. Accordingly, foreign private issuers still must comply with this updating requirement by a post-effective amendment or by incorporation by reference.

The SEC also did not modify Item 512(a)(2) (or Item 512(a)(3)). The issuer undertakings ensure that liability protection under the Securities Act remains in force throughout the life of the shelf registration statement (i.e., after the registration statement becomes effective). Item 512(a)(2) requires the issuer to agree that, for determining liability under the Securities Act, each post-effective amendment described in Item 512(a)(1) is deemed to be a new registration statement for the securities offered, and that each offering of those securities is deemed to be their initial bona fide offering. This extends the statute of limitations for investors in a delayed offering.⁷²

As part of the 2005 reforms, the SEC also amended Item 512(a) to include an undertaking (i.e., Item 512(a)(5)), in which the issuer agrees that information in a filed prospectus supplement is deemed part of the registration statement, and that a new effective date will be established for liability in shelf takedowns by the filing of a prospectus supplement, as set forth in Rules 430B and 430C (which are discussed later).

Further, as part of the 2005 reforms, the SEC adopted Rule 159A(a) which provides that, for determining liability under Section 12(a)(2) of the Securities Act, an issuer in a primary offering of securities, regardless of the form of the underwriting arrangement, will be a seller and will be considered to offer or sell the securities to a purchaser in the initial distribution of the securities by means of any of the following communications: (a) any preliminary prospectus or prospectus of the issuer for the offering required to be filed under Rule 424; (b) any issuer free writing prospectus; (c) the part of any other free writing prospectus for the offering containing issuer information; and (d) any other communication that is an offer in the offering made by the issuer to such purchaser. For issuers that file shelf registration statements, the SEC also adopted an undertaking to the same effect (i.e., Item 512(a)(6) of Regulation S-K).

⁷² Item 512(a)(3) requires the issuer to agree to remove from registration by post-effective amendment any securities registered for the shelf that remain unsold at the termination of the offering.

5. General Procedures

This section discusses the procedures for shelf category (x) (specifically, for foreign issuers eligible to use Form F-3 for primary offerings) before the reforms were adopted in 2005. As discussed in O. below, except for well-known seasoned issuers (“WKSIs”) using automatic shelf registration, these procedures generally still apply. Initially, a registration statement is prepared in advance of an offering. The shelf registration statement contains a “base prospectus” providing the same information about the issuer that is included in a regular prospectus, including information incorporated by reference from the issuer's last annual report on Form 20-F and subsequent Exchange Act filings.⁷³ The base prospectus contains only a general description of the categories of securities covered and the various possible methods of distribution.

For the greatest flexibility, a foreign issuer would file a registration statement describing generally various types of securities, denominated in several currencies and to be distributed by any one of several different underwriting methods, such as best efforts or firm commitment underwritings, agency placements and direct sales. In addition, the foreign issuer would file exhibits containing the agreements necessary to offer the securities, including proposed forms of the underwriting agreement and separate trust indentures for senior and subordinated debt securities listed in the registration statement. Shelf registration statements are declared effective without specific price figures, underwriting syndicate information and other information because the information is not known at the time of effectiveness.

To actually conduct an offering of some or all of the securities registered on the shelf, the issuer prepares a brief “prospectus supplement” for each specific offering when the terms of the offering are finalized. The prospectus supplement will specify the price, amount and method for distributing the securities being offered. The prospectus supplement provides all transaction-specific information that was omitted from the shelf registration statement when it became effective. Additionally, any material developments that have arisen after effectiveness or the last prospectus supplement filed with the SEC would also be described in the prospectus supplement. The prospectus supplement would be filed with the SEC and distributed to investors who purchased the securities,⁷⁴ neither of which would require any further SEC action.⁷⁵

⁷³ Even before the 2005 reforms were adopted, Item 512(a)(1) of Regulation S-K allowed Form F-3 foreign issuers to incorporate Exchange Act reports by reference to update shelf registration statements. As part of the 2005 reforms, the SEC amended Item 512(a)(1) to provide that, in shelf registration statements filed on Form S-3 (or F-3), all of the disclosures required by that Item may be made in any filed prospectus supplement or any Exchange Act report incorporated by reference into the registration statement, including through an incorporated Form 8-K (or 6-K).

Item 512(a)(4) of Regulation S-K allows Form F-3 issuers to incorporate Exchange Act reports by reference to update financial statements in accordance with Item 8.A of Form 20-F as well as other information necessary to keep the prospectus current. Item 512(a)(4) was not modified by the 2005 reforms.

⁷⁴ But see Securities Act Rule 172 (which was adopted as part of the 2005 reforms and provides that delivery of the final prospectus to investors is no longer required if certain conditions are met).

(a) Information in Base Prospectuses and Prospectus Supplements

As discussed above, before the securities offering reforms were adopted in 2005, a shelf registration statement at the time of effectiveness could contain a base prospectus which omitted information about the specific offering and the specific plan of distribution. When specific offerings were made using the base prospectus, a prospectus supplement containing this additional information would be distributed to investors and filed with the SEC.

Rule 430B under the Securities Act, which was adopted in 2005 as part of the securities offering reforms: (a) specifies the relationship between base prospectuses and prospectus supplements, and (b) clarifies what information should be included in a base prospectus and what may be in a prospectus supplement. Rule 430B, which generally applies only to offerings in shelf category (x) (i.e., primary offerings on Form S-3 or F-3), offerings by WKSIs registered on automatic shelf registration statements and secondary offerings by certain primary shelf eligible issuers, serves as a shelf offering corollary to Rule 430A under the Securities Act, which applies to non-shelf offerings.⁷⁶

Rule 430C under the Securities Act, which also was adopted as part of the 2005 reforms, covers: (a) all registered offerings that are not covered by Rule 430B, and (b) prospectuses that are not covered by Rule 430A.⁷⁷

Rule 430B codifies prior practices in most respects concerning the relationship between base prospectuses and prospectus supplements in offerings by issuers eligible to use Form S-3 or F-3 for primary offerings. Generally, under Rule 430B, the base prospectus for offerings in shelf category (x) (standard Form S-3 or F-3 primary offerings) may omit from the information required to be in the prospectus information that is unknown or not reasonably available to the issuer under Rule 409 under the Securities Act. For other than automatic shelf registration statements, the base prospectus still must include general descriptions of the types of securities and possible plans of distribution. As discussed later, Rule 430B also provides that issuers eligible to use Form S-3 or F-3 for primary offerings under General Instruction I.B.1 of those Forms may, in certain circumstances, omit from the base prospectus information about the identities of selling security holders and the amount of

Rule 424(c) expressly allows the filing of a prospectus supplement or sticker only, rather than requiring that the issuer using a prospectus supplement refile the entire prospectus with the supplement attached. However, a prospectus supplement that is distributed to investors ordinarily must be attached to the prospectus to which it relates.

⁷⁵ Nonetheless, the SEC has asked issuers with shelf registration statements for the issuance of new types of securities to submit their supplements for review before the securities are issued. To avoid after-the-fact review by the SEC, issuers usually comply, and if the SEC is concerned about the disclosure, the issuer would have to consider amending the supplement.

⁷⁶ Rule 430B also applies to offerings of mortgage-backed securities permitted by Rule 415(a)(1)(vii), which generally are registered on Form S-11 under the Securities Act.

⁷⁷ For example, issuers that are not primary shelf eligible, but that are eligible to register securities for resale on behalf of selling security holders under General Instruction I.B.3 of Form S-3 (or F-3) or to register the issuance of securities on exercise or conversion of outstanding securities under General Instruction I.B.4 of Form S-3 (or F-3) would not be eligible to rely on Rule 430B, but would instead be subject to Rule 430C.

securities to be sold by them. Rule 430B provides that a base prospectus that omits information as provided in the Rule will be a permitted Section 10 prospectus for Section 5(b)(1) of the Securities Act (i.e., for waiting period and post-effective period offers). Thus, after a registration statement is filed, offering participants can use a base prospectus that omits information in accordance with the Rule. Additionally, issuers and other offering participants can: (a) communicate using Rule 134 notices, and (b) use free writing prospectuses under Rules 164 and 433.

However, a base prospectus that omits statutorily required information is not a Section 10(a) (i.e., final) prospectus. To satisfy the requirements of Section 10(a), the issuer must provide the omitted information. Under Rule 430B, information that is unknown or not reasonably available to the issuer can later be added to the prospectus by means of: (a) a post-effective amendment to the registration statement; (b) a prospectus or prospectus supplement filed under Rule 424(b) that is deemed to be part of the registration statement; or (c) incorporation by reference from Exchange Act reports. Forms S-3 and F-3, as well as Item 512(a) of Regulation S-K, have also been amended to permit all information about the issuer and its securities required in the prospectus to be provided in a filed prospectus or prospectus supplement or incorporated by reference from Exchange Act reports.⁷⁸ For example, under the current rules, material changes to the plan of distribution can be included in an incorporated Exchange Act report or a prospectus supplement, while the rules in effect before the 2005 reforms were adopted required the filing of a post-effective amendment. Under Rule 430B, if omitted information that relates to an offering, such as the terms of the offering, the securities, the plan of distribution or any selling security holders (as opposed to issuer-related information) is included in an Exchange Act filing, a prospectus supplement must be prepared and filed under Rule 424 disclosing the specific Exchange Act report or reports in which the information is contained. Consequently, market practice generally has been to use a prospectus supplement. As was the case before the 2005 reforms were adopted, the prospectus supplement for each specific offering generally would include completed terms of the securities being offered, the price, the plan of distribution (including any underwriting or sales arrangements) and, where necessary, disclosure of material recent developments concerning the issuer not included in Exchange Act reports incorporated by reference. Additionally, as was the case before the 2005 reforms were adopted, the prospectus supplement must be filed with the SEC but no SEC action is required concerning the prospectus supplement.

(b) Post-Effective Identification of Selling Security Holders

Transfers of restricted securities can occur after a private placement is completed so that the identities of the holders of those restricted securities⁷⁹ at the time of filing the resale registration statement may not be known to the issuer.⁸⁰ Filing post-effective

⁷⁸ Issuers still have the flexibility to file post-effective amendments to include the information.

⁷⁹ Private placements and restricted securities are discussed in Chapters 6 and 7.

⁸⁰ Before the 2005 reforms were adopted, the SEC staff required all issuers registering securities for the benefit of selling security holders to include the names of selling security holders in the registration statement either before effectiveness or through a post-effective amendment to the registration statement, with limited exceptions for

amendments to add new or previously unidentified selling security holders can impose delays. To alleviate the timing concern arising from an issuer's inability to identify selling security holders before effectiveness, the current rules (adopted as part of the 2005 reforms) allow certain issuers to add the names of selling security holders and all information about them, as required by Item 507 of Regulation S-K or Item 9.D of Form 20-F, after effectiveness of the registration statement by: (a) a post-effective amendment to the registration statement; (b) a prospectus supplement (which will be deemed part of the registration statement for liability purposes); or (c) an Exchange Act report incorporated by reference into the registration statement (subject to filing a prospectus supplement identifying the report). First, under Rule 430B(b)(1), a WSKI may omit from the base prospectus in an automatic shelf registration statement the identity of any selling security holders and the amounts to be registered on their behalf. Additionally, under Rule 430B(b)(2), a base prospectus filed as part of a shelf registration statement for offerings under shelf category (i) (secondary shelves) by an issuer eligible to use Form S-3 or F-3 for primary offerings under General Instruction I.B.1 of those Forms (i.e., meeting the \$75 million public float requirement) can omit the identities of selling security holders and the amounts of securities to be registered on their behalf if all of the following conditions are met: (a) the resale registration statement refers to any unnamed selling security holders generically by identifying the initial offering in which the securities (or securities convertible into those securities) were sold;⁸¹ (b) the initial offering of the securities (or securities convertible into those securities) was completed; (c) the securities (or securities convertible into those securities) that are the subject of the resale registration statement were issued and outstanding before the original filing date of the resale registration statement; and (d) the issuer is not, and during the past three years neither the issuer nor any of its predecessors was, a blank check company, a shell company (other than a business combination related shell company) or an issuer in an offering of penny stock.

As discussed above, after effectiveness, the issuer may file a prospectus supplement to add the names of previously unidentified selling security holders and the amounts of securities they intend to sell. Any prospectus supplement that identifies selling security holders and the amounts to be sold by them that was previously omitted from the registration statement under Rule 430B must be filed with the SEC (or transmitted by a means reasonably calculated to result in filing) within two business days after the earlier of: (a) the date of sale, or (b) the date of first use.⁸²

the identities of selling security holders owning a de minimis amount of the issuer's securities (less than one percent) or receiving the securities as a result of a donative transfer.

⁸¹ The Rule requires disclosure of the initial offering in which the securities were sold, not any subsequent resale transaction (i.e., not any resale transaction in which any particular selling security holder may have acquired the securities). The goal of the disclosure is to clearly link the securities being registered for resale to a completed initial offering. See condition (b) in the text.

⁸² See Securities Act Rule 424(b)(7). As discussed below, the filing of a prospectus supplement to include the identity of omitted selling security holders under Rule 424(b)(7) will be deemed to be a new effective date of the registration statement for Section 11 liability purposes of the issuer and underwriter. Under the Securities Act, selling security holders may be underwriters in connection with the distribution of the securities being registered for resale on their behalf.

An issuer registering the resale of securities sold in a private offering may not rely on Rule 430B(b)(2) to identify after effectiveness selling security holders who will acquire the securities directly from the issuer if the securities are not yet issued in the private offering, even where the investors are contractually bound to acquire the securities.⁸³ The issuer can still register the resale of the not-yet-issued securities, but it must identify the selling security holders in the registration statement at the time of filing and before effectiveness because the issuer will know the identities of the selling security holders who will acquire the securities from it.

(c) Information Deemed Part of the Registration Statement

Rule 430B clarifies that information in a prospectus supplement will be deemed part of the related registration statement. Further, Rule 430C codifies similar provisions for shelf registrations by issuers not eligible to use Form S-3 or F-3 for primary offerings. As a result, a prospectus supplement will be considered part of the related registration statement for purposes of liability under Section 11 of the Securities Act as of the dates described below.

(d) Section 11 Liability for Prospectus Supplements

Before the 2005 reforms were adopted, only information included in a base prospectus or in an Exchange Act report that was incorporated by reference into a base prospectus was deemed to be included in a shelf registration statement. Prospectus supplements generally were thought not to be part of the registration statement or subject to Section 11 liability. Rule 430B (adopted as part of the 2005 reforms) clarifies that prospectus supplements and information in them will be deemed to be part of and included in a registration statement filed under shelf category (x) (primary shelf offerings on Form S-3 or F-3). Rule 430C (also adopted as part of the 2005 reforms) includes similar provisions for: (a) all offerings made other than under Rule 430B, and (b) prospectuses that are not covered by Rule 430A.⁸⁴ The information in the prospectus supplement, by virtue of being included in the registration statement, would become subject to Section 11 liability. As a result of Rules 430B and 430C, prospectus supplements required to be filed under Rule 424 will be deemed to be part of and included in registration statements for purposes of Section 11.

The date on which information in a prospectus supplement is deemed part of a registration statement depends on the purpose of the prospectus supplement. The date on which the information in a prospectus supplement will be deemed to be part of the related registration statement for purposes of Section 11 liability of issuers and underwriters only will be determined as follows:

- (a) for supplements filed in connection with most shelf takedowns, under Rule 430B, the earlier of: (i) the date that the supplement is

⁸³ These types of offerings include private investment in public equity (“PIPE”) transactions.

⁸⁴ Rule 430C applies to prospectuses filed in offerings made in reliance on Rule 430A to the extent the prospectus or prospectus supplement is not covered by Rule 430A.

first used,⁸⁵ or (ii) the date and time of the first contract of sale of securities to which the supplement relates;⁸⁶ and

- (b) for other supplements filed under Rule 430B or 430C, as applicable, as of the date the prospectus supplement is first used.

Rule 430B also establishes a new effective date for most delayed offerings, for purposes of shelf registration statement liability under Section 11, for: (a) the issuer, and (b) a person that is at the time an underwriter.⁸⁷ That new effective date is the date a prospectus supplement filed in connection with the takedown or takedowns is deemed part of the registration statement. Item 512(a)(5) of Regulation S-K (adopted as part of the 2005 reforms) requires issuers to agree to this additional Section 11 liability as of the dates described above.⁸⁸ The new effective date of the registration statement is relevant only for Section 11 liability. It is not considered the filing of a new registration statement for purposes of form eligibility. That determination will continue to be made at the time of the Section 10(a)(3) update to the registration statement (which typically occurs when the issuer files its annual report on Form 10-K or 20-F). Also, the new effective date does not affect the determination of when information is conveyed to a purchaser for Section 12(a)(2) liability purposes. Establishing a new effective date will not affect the information in the registration statement at the time of any prior sale, and the rights of an investor in a prior sale, with a previous effective date, will also be unaffected by any subsequently filed prospectus supplements or Exchange Act reports.

Rule 430B excludes from liability any directors or signing officers of the issuer and auditors or other experts as of a new effective date created by the filing of a prospectus supplement. Absent the filing of a prospectus supplement to provide updating information under Section 10(a)(3) or a prospectus supplement reflecting fundamental changes in the information in the registration statement, a prospectus supplement filing will not create a new effective date for directors or signing officers of the issuer. Similarly, the effective date for auditors and other experts will remain unchanged with the filing of a prospectus supplement, unless the prospectus supplement (or any Exchange Act report incorporated by reference into the

⁸⁵ The SEC's view is that the date of first use is not the date the prospectus supplement is given to a purchaser in connection with a sale, but instead, is the date that the prospectus is first available to the managing underwriter, a syndicate member or any prospective purchaser.

⁸⁶ Supplements as to which (a) in the text applies include: (1) supplements filed in connection with delayed primary offerings, and (2) supplements containing information concerning selling security holders omitted from the registration statement.

⁸⁷ This new effective date applies to: (1) delayed primary offerings, and (2) secondary offerings where the supplement contains information concerning selling security holders previously omitted from the registration statement.

Under Rule 430C, the filing of prospectus supplements will not trigger new effective dates of the registration statement.

⁸⁸ These rules (i.e., Rule 430B(f)(1) to (2) and Item 512(a)(5)) conform the effective date of Section 11 registration statement liability in most delayed offerings for issuers with such date for underwriters. Formerly, issuers had Section 11 liability as of the most recent effective date of the registration statement, whereas underwriter liability was assessed when the underwriter became an underwriter (which could be many months later).

prospectus or registration statement or any post-effective amendment) contains new audited financial statements, a new report or opinion or other information requiring the filing of a new consent under Section 7 of the Securities Act.

(e) Medium-Term Note Programs

After a shelf registration statement is effective, many foreign issuers dedicate at least part of the aggregate amount of securities registered for the shelf to a medium-term note program. The issuer and placement agents for the medium-term note program then prepare a prospectus supplement in accordance with Rule 424 for the entire planned amount of medium-term notes that describes the general terms of the notes and the specifics of the plan of distribution. As each medium-term note is sold, final maturity, interest rate and pricing information is disclosed in a sticker under Rule 424(c), which either is attached to the cover of the prospectus supplement or consists of a separate sheet. For shelf registration purposes, the sticker is a separate prospectus supplement. Therefore, like other prospectus supplements for shelf takedowns, it is filed with the SEC without any need for further SEC action. Additionally, the sticker is deemed to be part of the registration statement and triggers a new effective date.

O. Automatic Shelf Registration For WKSIs

1. Automatic Shelf Registration

Forms S-3 and F-3 and Rule 430B under the Securities Act allow an issuer that is a well-known seasoned issuer (“WKSI”) to register an unspecified amount of securities on a shelf registration statement without paying a filing fee when the registration statement is filed. This type of shelf registration statement, called an “automatic shelf registration statement,” becomes automatically effective and sales can take place immediately after filing, without SEC review.

Under automatic shelf registration, any registrant that is an eligible WKSI may use Form S-3 or F-3 to file an immediately effective shelf registration statement for offerings of most types of securities and certain securities of its majority-owned subsidiaries (including unconditional guarantees of the parent’s securities).⁸⁹ An issuer must test its eligibility for automatic shelf registration on the latest of: (a) the filing of the issuer’s most recent shelf registration statement, (b) the most recent amendment to its shelf registration statement for satisfying Section 10(a)(3) of the Securities Act, and (c) the date of filing of the issuer’s most recent annual report on Form 10-K or 20-F (if it has not filed a shelf registration statement for the prior 16 months). Consequently, an issuer must test its eligibility for automatic shelf

⁸⁹ An issuer qualifying as a WKSI under the \$1 billion debt test generally is limited in the types of securities that it may register on an automatic shelf registration statement. Specifically, such an issuer may register only non-convertible securities, other than common equity, and certain full and unconditional guarantees unless the issuer also is eligible to register a primary offering on Form S-3 or F-3 under General Instruction I.B.1 of those Forms (i.e., has a worldwide common equity public float of at least \$75 million). If the issuer meets the \$75 million public float requirement, it also may register common equity on its automatic shelf registration statement. In either case, the issuer is permitted to register only offerings for cash (i.e., an automatic shelf registration statement cannot be used to register exchange offers or other business combination transactions).

registration both on the initial filing date and at the time of each annual Section 10(a)(3) update (which typically occurs when the issuer files an incorporated annual report on Form 10-K or 20-F).

2. Immediate Effectiveness of an Automatic Shelf Registration Statement and Proper Form: Rules 462 and 401

Under Rule 462(e) under the Securities Act, an automatic shelf registration statement and any post-effective amendment to it (including an amendment to add additional classes of securities under Rule 413(b) under the Securities Act) becomes effective immediately upon filing with the SEC. Under Rule 401(g) under the Securities Act, an automatic shelf registration statement will be deemed to be on the proper form unless the SEC notifies the issuer of its objection to the use of the form.

3. Information Omitted From an Automatic Shelf Registration Statement: Rule 430B

Under Rule 430B under the Securities Act, a prospectus filed as part of an automatic shelf registration statement (i.e., a base prospectus) may omit:

- (a) information that is unknown or not reasonably available to the issuer (under Rule 409 under the Securities Act);
- (b) whether the offering is a primary offering, a secondary offering, or both;
- (c) the plan of distribution for the securities;
- (d) a description of the securities registered, other than identifying the name or class of the securities;
- (e) the identity of other issuers; and
- (f) the names of any selling security holders and amounts of securities to be registered on their behalf.

Rule 430B provides that virtually all of the omitted information can be included in a post-effective amendment to the registration statement, in a prospectus supplement filed under Rule 424(b) under the Securities Act or by incorporation by reference of Exchange Act reports. However, an issuer adding new types of securities or new registrants must do so by immediately effective post-effective amendments (which requires appropriate signature pages, Exhibit 5 opinions and consents).

4. Adding New Classes of Securities to an Automatic Shelf Registration Statement After Effectiveness: Rule 413(b)

Under Rule 413(b) under the Securities Act, a WCSI may add new classes of securities (and certain securities of its majority-owned subsidiaries) to an effective automatic shelf registration statement through a post-effective amendment. That post-effective amendment will become effective automatically upon filing (under Rule 462). Details about the new class of

securities to be offered can be provided via a post-effective amendment, a prospectus supplement or an incorporated Exchange Act report.

5. Pay-As-You-Go Registration Fees For an Automatic Shelf Registration
Statement: Rules 456 and 457

Under Rules 456(b)(1) and 457(r) under the Securities Act, WKSIs registering securities using the automatic shelf registration process may defer paying filing fees until the time of the actual offering when a prospectus supplement under Rule 424(b) is due. For each shelf takedown, a WKSI will include the amount of the pay-as-you-go registration fee (in the “Calculation of Registration Fee” table) either in a Rule 424(b) prospectus or in a post-effective amendment filed at the time of fee payment.

An automatic shelf registration statement relying on pay-as-you-go registration fee payment will be considered filed upon receipt by the SEC, and the securities will be considered registered if the fee has been paid and the post-effective amendment or Rule 424(b) prospectus including the revised “Calculation of Registration Fee” table has been filed.

CHAPTER 4.

FORMS OF REGISTRATION STATEMENTS

The SEC has published numerous forms and rules which specify the information required by a registration statement. The forms used by various issuers are discussed below.

A. Forms of Registration Statements for U.S. Issuers

The forms used by U.S. companies are as follows:

1. Form S-1: Long Form Registration Statement

Form S-1 is the most commonly used form of registration statement. For non-reporting issuers (essentially, issuers conducting an IPO), this registration statement and the related prospectus must contain a complete description of the Company's business, the securities to be issued and the terms of the offering. For reporting issuers, Form S-1 may incorporate by reference previously filed Exchange Act reports (known as "historical" incorporation by reference). This Form requires three years audited financial statements, unaudited financial statements for the interim "stub" period and five years summary financial information.

Form S-1 is used for registration under the Securities Act of securities of all registrants for which no other form is authorized or prescribed, except that it may not be used for securities of foreign governments or their political subdivisions. For example, Form S-1 may be used by a U.S. company or a foreign private issuer to register an offering of non-investment grade asset-backed securities.

2. Form S-3: Short Form Registration Statement

Form S-3 permits extensive (including "forward") incorporation by reference to Exchange Act reports and generally requires that only information relating to the specific offering be included in the prospectus. All other disclosures may be provided by incorporation by reference to the company's Form 10-K (Exchange Act annual report), Form 10-Q (Exchange Act quarterly report), Form 8-K (Exchange Act current report) and the proxy statements. Form S-3 enables a company to conduct a continuous primary offering for up to three years "off the shelf" under Rule 415 under the Securities Act. Form S-3 is available if certain registrant and transaction requirements have been met.

(a) Registrant Requirements

Form S-3 is available if the issuer has been a reporting company under the Exchange Act (i.e., a reporting issuer) for at least 12 months, has made all filings in a timely manner for the last 12 months, and, since the end of the most recent fiscal year for which a Form 10-K annual report has been filed, has not defaulted on a preferred dividend or sinking fund payment, payment of any indebtedness or long-term lease rentals, which defaults in the aggregate are material to the financial position of the issuer.

(b) Transaction Requirements

Additionally, the offering must fit within one of the applicable transaction requirements. Form S-3 may be used to register any debt or equity offered for cash in primary offerings by or on behalf of the issuer or in secondary offerings by a person other than the issuer if the aggregate market value of the voting and non-voting common equity held by non-affiliates (i.e., the “public float”) is \$75 million or more.

General Instruction I.B.6 of Form S-3 permits the use of Form S-3 by an issuer with less than a \$75 million public float to register primary offerings of its securities for cash if it:

- (i) has a class of common equity securities that is listed and registered on a national securities exchange,
- (ii) does not sell more than one-third of its public float in primary offerings under General Instruction I.B.6 over the previous 12 calendar months, and
- (iii) has not been a shell company for at least 12 calendar months before filing the registration statement.

Form S-3 may also be used where the public float is less than \$75 million, including some transactions for primary offerings for cash of investment grade non-convertible debt or preferred stock, rights offerings, dividend or interest reinvestment plans and conversions, warrants and options. Additionally, the requirement of a \$75 million float need not be satisfied (i) in secondary offerings by someone other than the issuer if the class of securities is listed and registered on a national securities exchange; or (ii) in offerings of investment grade asset-backed securities for cash.

3. Contents of the Form S-1 or Form S-3 Prospectus

The prospectus should be in plain English and contain, among other matters, information concerning the following: (i) the issuer, (ii) risk factors, (iii) dilution, (iv) shares subject to options, warrants and convertibles, (v) related party transactions, (vi) anti-takeover provisions, (vii) management’s discussion and analysis of financial condition and results of operations (“MD&A”), (viii) use of proceeds, (ix) management, (x) significant beneficial owners, and (xi) plan of distribution.

4. Form S-4: Business Combinations and Exchange Offers

Form S-4 may be used to register securities to be issued: (1) in a business combination of the type specified in Rule 145(a) under the Securities Act;⁹⁰ (2) in a merger in

⁹⁰ The thrust of Rule 145 is that an offer or sale of securities occurs when there is submitted to security holders a plan or agreement under which the holders are required to elect, on the basis of what is in substance a new investment decision, whether to accept a new or different security in exchange for their existing security. Accordingly, Rule 145(a) provides that an offer or sale will be involved, within the meaning of Section 2(a)(3) of

which the applicable state law would not require the solicitation of the votes or consents of all of the security holders of the company being acquired; (3) in an exchange offer for securities of the issuer or another entity; (4) in a public reoffering or resale of any such securities acquired under the registration statement; or (5) in more than one of the kinds of transactions listed in (1) through (4) registered on one registration statement. Form S-4 may not be used if the registrant is a registered investment company or a business development company.

If the registrant meets the requirements of and elects to comply with the provisions in any item of Form S-4 or Form F-4 (discussed below) that provides for incorporation by reference of information about the registrant or the company being acquired, the prospectus must be sent to the security holders no later than 20 business days before the date on which the meeting of such security holders is held or, if no meeting is held, at least 20 business days before either: (1) the date of such votes, consents or authorizations; or (2) the date the transaction is consummated or the votes, consents or authorizations may be used to effect the transaction. Attention is directed to Sections 13(e), 14(d) and 14(e) of the Exchange Act and the rules and regulations thereunder regarding other time periods for exchange offers and going private transactions.

5. Form S-8: Simplified Form For Employee Stock Offerings

As one alternative to full registration under the Securities Act, eligible U.S. (or foreign) issuers may register employee stock offerings on Form S-8, a simplified registration form.

(a) Eligible Issuers

A U.S. (or foreign) issuer is eligible to use Form S-8 if:

- (i) immediately before filing the registration statement, the issuer is required to file reports under Section 13(a) or 15(d) of the Exchange Act (i.e., is a reporting issuer);
- (ii) the issuer has filed all required Exchange Act reports and other materials during the preceding 12 months (or for such shorter period that the issuer has been a reporting issuer);
- (iii) the issuer is not a shell company and has not been a shell company for at least 60 calendar days before filing the registration statement; and
- (iv) if the issuer has been a shell company at any time, it has filed current "Form 10 information" with the SEC at least 60 calendar

the Securities Act, so far as the security holders of a corporation or other person are concerned where, under statutory provisions of the jurisdiction under which the corporation or other person is organized, or under provisions contained in its certificate of incorporation or similar controlling instruments, or otherwise, there is submitted for the vote or consent of the security holders a plan or agreement of: (i) merger or consolidation (accompanied by an exchange of securities), (ii) asset transfer (accompanied by a distribution of securities), or (iii) reclassification (involving the substitution of one security for another).

days previously reflecting its status as an entity that is not a shell company (as used here, “Form 10 information” means the information required by Form 10 or 20-F to register under the Exchange Act each class of securities being registered on the Form S-8).

(b) Eligibility of Transaction

Form S-8 permits an eligible U.S. (or foreign) issuer to register: (i) securities to be offered under an employee benefit plan to its employees or to employees of its parents or subsidiaries, and (ii) interests in the plan (where interests in the plan are securities). Form S-8 is not available for use in a capital-raising transaction.

Form S-8 may also be used for the exercise of employee benefit plan options, and the later resale of the underlying securities, by an employee’s family member that acquired the options through a gift or a domestic relations order. However, Form S-8 may not be used for the exercise of options transferred for value.

6. Form S-11: Securities Issued By Real Estate Companies

Form S-11 is used for registration under the Securities Act of: (a) securities issued by a real estate investment trust; or (b) securities issued by other issuers whose business is primarily that of acquiring and holding for investment real estate or interests in real estate or interests in other issuers whose business is primarily that of acquiring and holding real estate or interests in real estate for investment. (However, Form S-11 may not be used: (a) by investment companies registered or required to register under the Investment Company Act, or (b) for offerings of asset-backed securities.) Form S-11 may incorporate by reference previously filed Exchange Act reports.

7. Scaled Disclosure Requirements For Smaller Reporting Companies

Smaller reporting companies using Form S-1, S-3, S-4, S-8, or S-11 qualify for scaled disclosure requirements. A “smaller reporting company” is defined in Rule 405 under the Securities Act as an issuer that is not an investment company, an asset-backed issuer or a majority-owned subsidiary of a parent that is not a smaller reporting company, and that:

- (1) had a public float of less than \$75 million as of the last business day of its most recently completed second fiscal quarter (computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates by the price at which the common equity was last sold, or the average of the bid and asked prices of the common equity, in the principal market for the common equity); or
- (2) for an initial registration statement under the Securities Act or Exchange Act for shares of its common equity, had a public float of less than \$75 million as of a date within 30 days of the date of filing the registration statement (computed by multiplying the aggregate worldwide number of such shares held by non-affiliates before the registration plus, in the case of a Securities

Act registration statement, the number of such shares included in the registration statement by the estimated public offering price of the shares); or

- (3) for an issuer whose public float as calculated under paragraph (1) or (2) of this definition was zero, had annual revenues of less than \$50 million during the most recently completed fiscal year for which audited financial statements are available.

Foreign companies can take advantage of the regime for smaller reporting companies (discussed below) if they: (a) meet the above definition of “smaller reporting company”; (b) choose to file on U.S. company forms (instead of the special forms for foreign private issuers); and (c) provide financial statements prepared in accordance with U.S. GAAP. (Formerly, the only foreign companies permitted to use SEC scaled disclosure requirements were Canadian companies.)

Smaller reporting companies prepare and file their SEC registration statements and reports using the standard forms for U.S. companies (e.g., Forms S-1 and 10-K), though the information required to be disclosed may differ. For U.S. companies, Regulation S-X contains the SEC requirements for financial statements, while Regulation S-K contains the non-financial disclosure requirements. To locate the scaled disclosure requirements, smaller reporting companies must refer to Article 8 of Regulation S-X and the special paragraphs labeled “smaller reporting companies” in Regulation S-K.

Smaller reporting companies may choose to comply with scaled or non-scaled financial and non-financial item requirements on an item-by-item (i.e., “a la carte”) basis in any one filing. However, where the smaller reporting company requirement is more rigorous, the company must meet the more rigorous standard. Currently, the smaller reporting company requirements under Item 404 of Regulation S-K (transactions with related persons, promoters and certain control persons) are the only place where the scaled requirements can be more rigorous than the larger company standard.

8. Form 1-A: Regulation A Exemption For Small Offerings

Regulation A (i.e., Rules 251-263) under the Securities Act is an exemption from Securities Act registration that works like a registered offering with an offering statement similar to a registration statement and an offering circular similar to a prospectus. Expenses under Regulation A are lower than for a registered offering. Non-reporting companies may use Form 1-A to conduct public offerings under Regulation A of up to \$5 million in a 12-month period, \$1.5 million of which may be sales of securities by stockholders. Regulation A is not available to reporting companies.

B. Forms of Registration Statements for Foreign Private Issuers

The following forms of registration statements were designed for foreign private issuers:

1. Form F-1: Long Form Registration Statement

Like Form S-1 for U.S. issuers, Form F-1 is the general form for foreign private issuers. It is available to any foreign private issuer when no other form is available. (However,

Form F-1 may not be used for an offering of asset-backed securities.) The information required by Form F-1 is generally the same information required by Form F-3, except that Form F-1 only permits incorporation by reference of previously filed Exchange Act reports (i.e., historical incorporation by reference). This registration statement must contain: (i) the information required by Part I of Form 20-F; (ii) financial statements that comply with Item 18 of Form 20-F (i.e., fully reconciled to U.S. GAAP and Regulation S-X), where the financial statements are not prepared in accordance with U.S. GAAP or IFRS as issued by the IASB; and (iii) information concerning significant business combinations. (For an issuer's fiscal years ending before December 15, 2011, financial statements that comply with the less demanding reconciliation of Item 17 of Form 20-F are permitted in certain limited cases.)

2. Form F-3: Short Form Registration Statement

Like Form S-3 for U.S. issuers, Form F-3 is the most exclusive of the forms for foreign private issuers. Foreign private issuers eligible to use Form F-3 rely on the incorporation by reference (including "forward" incorporation) into the registration statement and prospectus of the issuer's latest Form 20-F and other Exchange Act reports. Otherwise, Form F-3 generally requires transaction-related information. Issuers eligible to register securities for primary offerings using Form F-3 short form registration may use Form F-3 for shelf registration. Form F-3 may not be used for an offering of asset-backed securities.

(a) Eligible Issuers

To be eligible to use Form F-3, an issuer must be a foreign private issuer that meets the requirements set forth below to register securities offered in an eligible transaction, as described below.

- (i) The issuer must be reporting under the Exchange Act and have filed at least one annual report on Form 20-F, 10-K or 40-F for a Canadian issuer;
- (ii) The issuer must have been subject to those Exchange Act reporting requirements and made all filings timely during the last 12 calendar months; and
- (iii) Since the end of the last fiscal year for which audited financial statements of the issuer and its consolidated subsidiaries were included in an Exchange Act report, neither the issuer nor any of its subsidiaries have defaulted on any dividend or sinking fund installment on preferred stock, or on any loan or long-term lease payment (which defaults in the aggregate are material to the financial position of the issuer and its subsidiaries, taken as a whole).

(b) Eligible Transactions

- (i) For primary offerings for cash, an eligible issuer may use Form F-3 if: (A) its public float (i.e., the market value of its voting and non-

voting common equity held by non-affiliates) is \$75 million or more; and (B) its latest Form 20-F, 10-K or 40-F annual report contains financial statements that comply with Item 18 of Form 20-F (i.e., full reconciliation to U.S. GAAP), where the financial statements are not prepared in accordance with U.S. GAAP or IFRS as issued by the IASB.

- (ii) For primary offerings for cash, an eligible issuer may use Form F-3 if it has a public float of less than \$75 million if it:
 - (A) has a class of common equity securities that is listed and registered on a national securities exchange,
 - (B) does not sell more than one-third of its public float in primary offerings under this provision of Form F-3 (i.e., General Instruction I.B.5 of Form F-3) over the previous 12 calendar months, and
 - (C) has not been a shell company for at least 12 calendar months before filing the registration statement.
- (iii) For secondary offerings, affiliates may use Form F-3 to register securities for resale, and the required financial statements must also comply with Item 18 of Form 20-F (where the financial statements are not prepared in accordance with U.S. GAAP or IFRS as issued by the IASB).
- (iv) For certain rights offerings, dividend or interest reinvestment plans, conversions of convertible securities and exercises of warrants, an eligible issuer may use Form F-3 if it has a public float of less than \$75 million; in these limited cases, for an issuer's fiscal years ending before December 15, 2011, financial statements that comply with the less demanding reconciliation of Item 17 of Form 20-F are permitted.

(c) Information Required

Form F-3 requires an issuer to provide information concerning: (i) the offering, including a summary of the information contained in the prospectus (where appropriate), risk factors, ratio of earnings to fixed charges, use of proceeds, determination of the offering price, dilution, selling security holders, plan of distribution, securities to be registered, and interests of named experts and counsel; (ii) the issuer, through incorporation by reference to: (1) its latest Exchange Act annual report on Form 20-F (or 10-K or 40-F) or its latest Exchange Act registration statement on Form 10, (2) its subsequent annual and other subsequent periodic reports filed under the Exchange Act before the termination of the offering, and (3) if appropriate, Form 6-K; (iii) material changes in the issuer's affairs since the end of the fiscal year covered by the latest Exchange Act annual report, where that information has not been described in subsequent interim reports under the Exchange Act (such as a report on Form 6-K,

10-Q or 8-K) that are incorporated by reference; and (iv) financial statements of businesses recently acquired or likely to be acquired, and financial information required because of a material disposition of assets outside the normal course of business.

(d) Delivery of Incorporated Information

Form F-3 requires that the issuer provide to persons to whom a prospectus is delivered, on request and without charge, a copy of the information incorporated by reference in the prospectus but not delivered with the prospectus. Where the financial statements in the Form 20-F annual report, which is incorporated by reference into the subject Form F-3, are not current enough to comply with Regulation S-X, current financial statements that do comply must be included directly in the prospectus or incorporated by reference from a Form 6-K or an amended Form 20-F (or 10-K or 40-F).

3. Form F-4: Business Combinations and Exchange Offers

Form F-4 may be used by any foreign private issuer for registration under the Securities Act of securities to be issued: (1) in a business combination of the type specified in Rule 145(a); (2) in a merger in which the applicable law would not require the solicitation of the votes or consents of all of the security holders of the company being acquired; (3) in an exchange offer for securities of the issuer or another entity; (4) in a public reoffering or resale of any such securities acquired under the registration statement; or (5) in more than one of the kinds of transactions listed in (1) through (4) registered on one registration statement. Form F-4 may not be used if the registrant is a registered investment company.

If the registrant meets the requirements of and elects to comply with the provisions in any item of Form F-4 or Form S-4 that provides for incorporation by reference of information about the registrant or the company being acquired, the prospectus must be sent to the security holders no later than 20 business days before the date on which the meeting of such security holders is held or, if no meeting is held, the earlier of 20 business days before either: (1) the date the votes, consents or authorizations may be used to effect the corporate action; or (2) if votes, consents or authorizations are not used, the date the transaction is consummated. Attention is directed to Sections 13(e), 14(d) and 14(e) of the Exchange Act and the rules and regulations thereunder regarding other time periods for exchange offers and going private transactions.

4. Form F-6: American Depositary Receipts

Form F-6 is a special form used to register under the Securities Act American Depositary Receipts (“ADRs”) issued by a depositary against the deposit of securities of a foreign issuer. An ADR is a negotiable certificate, a receipt, issued by a U.S. depositary (typically, a U.S. bank or trust company) that represents ownership of securities of a foreign issuer. These securities (typically equity securities) are deposited by their holder in the depositary or in its foreign correspondent or affiliate. An ADR may represent one foreign security or a fraction or multiple of a foreign security. ADRs are issued to avoid the problems associated with owning foreign securities (e.g., collecting dividends and transfer problems) and trade in the U.S. securities market like U.S. securities.

For the Securities Act, ADRs and the underlying deposited securities are each considered a separate security. Accordingly, each must be registered unless an exemption applies. The issuer registers the deposited securities and the depositary registers the ADRs. The deposited securities may be registered on Form F-1, F-3 or F-4 (whichever is applicable), but not on Form F-6. While ADRs may be registered on Form F-6, they may also be registered on any form used to register the deposited securities, provided that the registration statement conforms to Form F-6 and either the depositary or "the legal entity created by the agreement for the issuance of ADRs" signs the registration statement with respect to the disclosure and undertakings made in response to the requirements of Form F-6.

ADRs registered on Form F-6, but not the underlying deposited securities, are exempt from registration under Section 12 of the Exchange Act.

C. Forms of Registration Statements for MJDS Offerings of Canadian Companies

1. Introduction

The Multijurisdictional Disclosure System ("MJDS") permits qualified Canadian issuers to offer their securities to U.S. investors based on disclosure documents prepared under Canadian law. The MJDS also covers the filing of continuous disclosure information and the registration of exchange offers and business combinations.

Under the MJDS, qualified Canadian issuers comply with the registration requirement of the Securities Act by: (i) filing a Canadian disclosure document with the appropriate Canadian regulatory body, and (ii) filing the same material (with some additional disclosure for U.S. investors) with the SEC under cover of a "wrap around" MJDS registration form. Under certain MJDS forms, the prospectus must contain a reconciliation to U.S. GAAP. Typically, the SEC does not review the form in reliance on the Canadian review.

2. Forms

The SEC has adopted five MJDS forms (Forms F-7, F-8, F-80, F-9 and F-10) to assist Canadian issuers registering securities under the Securities Act. The SEC's rules for "plain English" do not apply to these MJDS forms.

(a) Form F-7: Rights Offerings

Form F-7 is available to register securities offered for cash upon the exercise of rights that are granted pro rata to existing shareholders.

Form F-7 is available to an issuer that:

- (i) is a Canadian foreign private issuer;
- (ii) has had a class of securities listed for 12 months on The Montreal Exchange, The Toronto Stock Exchange, or the Senior Board of the Vancouver Stock Exchange before filing; and
- (iii) has been subject to Canadian reporting requirements for 36 months before filing, and is currently in compliance with those requirements.

For Form F-7 there is no substantiality, i.e., “public float,” requirement and no requirement to reconcile financial statements to U.S. GAAP. Nor do the U.S. accountant independence rules apply. However, if the rights granted U.S. holders are transferable other than under Regulation S under the Securities Act, then the securities underlying the rights may not be registered on Form F-7.

Form F-7 may not be used if the issuer is an investment company registered or required to be registered under the Investment Company Act.

(b) Forms F-8 and F-80: Exchange Offers and Business Combinations

(i) Introduction

Forms F-8 and F-80 are used to register securities offered in exchange offers and business combinations. These forms may be used regardless of whether the securities are the sole consideration for the exchange offer or business combination, or whether they are offered with cash. Forms F-8 and F-80 are intended to encourage Canadian issuers to extend exchange offers and business combinations to U.S. security holders. For an exchange offer, Form F-8 requires that less than 25% of the class of securities sought in the exchange offer be held by U.S. holders. For a business combination, Form F-8 requires that less than 25% of the class of securities to be offered by the successor issuer be held by U.S. holders, measured as if the business combination were completed. Form F-80 is identical to Form F-8 except that Form F-80 imposes a 40% ceiling on U.S. ownership instead of a 25% ceiling.

(ii) Conditions

Both Forms F-8 and F-80 are available to an issuer that meets the following general conditions:

- (A) the issuer must prepare a takeover bid circular or issuer bid circular (if an exchange offer) or an information circular (if a business combination) under the requirements of a Canadian jurisdiction and cannot be exempt from those disclosure requirements; and
- (B) the securities to be registered must be offered to U.S. holders on terms and conditions no less favorable than those offered to any other holder of the same class of securities.

Plus, the issuer must:

- (C) be a Canadian foreign private issuer;
- (D) have had a class of securities listed on The Montreal Exchange, The Toronto Stock Exchange or the Senior Board of the Vancouver Stock Exchange for at least 12 months before filing;
- (E) have been subject to Canadian reporting requirements for 36 months before filing;
- (F) be in current compliance with those listing and reporting requirements; and
- (G) have a public float (i.e., a market value of equity shares held by non-affiliates) of Canadian (CDN) \$75 million or more (except where the issuer is making an exchange offer for its own securities, in which case there is no public float requirement or, for a business combination, except under certain circumstances involving a participating company that was the subject of an exchange offer or cash tender offer during the past 12 months).

For an exchange offer, the issuer of the securities to be exchanged i.e., the target, must also be a Canadian foreign private issuer.

For a business combination: (1) each participating company (including the successor issuer) must be a Canadian foreign private issuer; and (2) each participating company (other than small nonqualified participating companies and the successor issuer) must meet the listing, reporting and public float requirements discussed in (D) through (G) above. To not preclude use of the MJDS when a smaller company is participating in a business combination, Form F-8 (and Form F-80) does not impose a listing, reporting or public float requirement on any participating company if those requirements are met by other participating companies whose assets and gross revenues from continuing operations, respectively, would contribute at least 80% of the successor issuer's total assets and gross revenues from continuing operations, as measured based on pro forma combination of the participating companies' most recently completed fiscal years.

Additionally, the MJDS provides a safe harbor for a participating company that cannot meet the public float requirement. Specifically, Form F-8 (and Form F-80) may be used for second-step business combinations occurring within 12 months after an exchange offer or cash tender offer. In that case, if the participating company's equity shares offered in the exchange offer or cash tender offer were registered or could have been registered on Form F-8, F-9, F-10 or F-80, or if Schedule 13E-4F or 14D-1F were filed or could have been filed in the transaction, the company will be deemed to meet the public float requirement of Form F-8 (or Form F-80) for the business combination if that requirement would have been met by the company immediately before commencement of the exchange offer or cash tender offer.

Otherwise, the reduction in that participating company's public float resulting from the prior offer might prevent it from meeting the public float requirement for the second-step business combination.

Forms F-8 and F-80 may not be used if the registrant or, in the case of an exchange offer, the target is an investment company registered or required to be registered under the Investment Company Act.

(iii) Financial Statements

The financial statements in Forms F-8 and F-80 need not be reconciled to U.S. GAAP, but the U.S. accountant independence rules do apply.

(c) Form F-9: Investment Grade Securities

(i) Introduction

Form F-9 may be used to register offerings of investment grade debt securities or investment grade preferred securities that: (A) are offered for cash or in an exchange offer; and (B) are either non-convertible or are convertible only after one year from the date of issuance (and, except in the case of guaranteed securities, as discussed below, are thereafter only convertible into a security of another class of the issuer). A security is “investment grade” if, at the time of its sale, at least one nationally recognized statistical rating organization (“NRSRO”) in the United States or at least one Canadian approved rating organization (“ARO”) has rated the security in one of its investment grade categories.

Form F-9 may not be used if no takeover bid circular or issuer bid circular (for an exchange offer) or prospectus (in all other cases) is prepared under the requirements of any Canadian jurisdiction due to the availability of an exemption from those requirements. Additionally, Form F-9 may not be used if the registrant or, in the case of an exchange offer, the issuer of the securities to be exchanged (i.e., the target) is an investment company registered or required to be registered under the Investment Company Act.

(ii) Conditions

Form F-9 is available to a Canadian issuer that:

- (A) is a foreign private issuer or a crown corporation;
- (B) has an aggregate market value of the public float of its outstanding equity shares of U.S. \$75 million or more; and
- (C) has been subject to Canadian reporting requirements for at least 12 months before filing and is currently in compliance with those requirements.

If the securities offered are not convertible, then the public float requirement does not apply.

Under the MJDS, a majority-owned subsidiary of an eligible Canadian issuer may offer debt or preferred securities on Form F-9. Like Form F-10, Form F-9 is available for certain issuers of guaranteed securities. A majority-owned Canadian subsidiary issuing investment grade debt or preferred securities need not meet the 12-month reporting requirement or the public float requirement (where applicable) if the securities are fully and unconditionally guaranteed by a parent that is eligible to use Form F-9. In other words, if the majority-owned subsidiary (A) is organized or incorporated under the laws of Canada or a Canadian province or territory, and (B) is a foreign private issuer or a crown corporation, the subsidiary will be deemed to meet the reporting and public float requirements of Form F-9 if its parent: (A) meets all of the Form F-9 eligibility requirements, and (B) fully and unconditionally guarantees the securities being registered as to principal and interest (if debt securities) or as to liquidation preference, redemption price and dividends (if preferred securities). The securities being registered by the majority-owned subsidiary may be convertible or exchangeable, but only after one year from the date of issuance and only for securities of the parent.

(iii) Exchange Offers

Form F-9 is available not only to register financings under the Securities Act, but also for exchange offers. To use Form F-9 to register an exchange offer, certain additional requirements must be met. First, the target issuer must: (A) be incorporated or organized under the laws of Canada or a Canadian province or territory, and (B) be a foreign private issuer or a crown corporation. Second, the securities to be registered on Form F-9 must be offered to U.S. holders on terms and conditions no less favorable than those offered to any other holder of the same class of securities to be exchanged (the “subject securities”) for the securities of the registrant.

(iv) Financial Statements

The financial statements included in the Form F-9 registration statement need not be reconciled to U.S. GAAP, but the U.S. accountant independence rules do apply.

(d) Form F-10: General Registration Form

(i) Introduction

Form F-10 may be used for Securities Act registration of any security, including common shares, non-investment grade (i.e., high-yield) debt or preferred shares, and debt or preferred shares that may be converted within one year of issuance. Form F-10 is the only Securities Act registration form in the MJDS that requires issuers to provide financial information reconciled to U.S. GAAP (under Item 18 of Form 20-F) and for which the U.S. accountant independence rules apply.

(ii) Conditions

Form F-10 may only be used if a takeover bid circular or issuer bid circular (for an exchange offer), an information circular (for a business combination), a rights offering circular (for an exempt rights offering), or a prospectus (in all other cases) is prepared

under the requirements of any Canadian jurisdiction. If this condition is met, an issuer may use Form F-10 if it:

- (A) is a Canadian foreign private issuer;
- (B) has been subject to Canadian reporting requirements for at least 12 months before filing and is currently in compliance with those requirements; and
- (C) has a public float (i.e., a market value of outstanding equity held by non-affiliates) of U.S. \$75 million.

For an issuer that is the successor to a business combination that occurred within the previous 12 months to be eligible, the issuer and predecessors that contributed 80% of assets and gross revenues from continuing operations must together satisfy the 12-month reporting requirement. In other words, the successor issuer will be deemed to meet the 12-month reporting requirement discussed in (B) above if: (1) the time that the successor issuer has been a reporting issuer in Canada, when added separately to the time that each predecessor participating company (other than small nonqualified participating companies) had been a reporting issuer in Canada as of the business combination, in each case equals at least 12 months; and (2) the successor issuer has been subject to those reporting requirements since the business combination and currently is in compliance with its obligations under those requirements.

If Form F-10 is used for an exchange offer, the target issuer must be a Canadian foreign private issuer. Similarly, if Form F-10 is used for a business combination, each participating company, including any small nonqualified participating company, must be a Canadian foreign private issuer. In either case, the securities to be registered on Form F-10 must be offered to U.S. holders on terms and conditions no less favorable than those offered to any other holder of the same class of the target securities (if an exchange offer) or the securities of the participating company (if a business combination).

For a business combination, each participating company (other than small nonqualified participating companies and the successor issuer) must meet the reporting and public float requirements discussed in (B) and (C) above. To not preclude use of the MJDS when a smaller company is participating in a business combination, Form F-10 does not impose a reporting or public float requirement on any participating company if those requirements are met by other participating companies whose assets and gross revenues from continuing operations, respectively, would contribute at least 80% of the successor issuer's total assets and gross revenues from continuing operations, as measured based on pro forma combination of the participating companies' most recently completed fiscal years.

Additionally, Form F-10 provides a safe harbor where a participating company cannot meet the public float requirement. Specifically, Form F-10 also may be used for second-step business combinations occurring within 12 months after an exchange offer or cash tender offer. In that case, if the participating company's equity shares offered in the exchange offer or cash tender offer were registered or could have been registered

on Form F-8, F-9, F-10 or F-80, or if Schedule 13E-4F or 14D-1F were filed or could have been filed in the transaction, the company will be deemed to meet the public float requirement of Form F-10 for the business combination if that requirement would have been met by the company immediately before commencement of the exchange offer or cash tender offer. Otherwise, the reduction in that participating company's public float resulting from the prior offer might prevent it from meeting the public float requirement for the second-step business combination.

Form F-10 may not be used if the registrant or, in the case of an exchange offer, the issuer of the securities to be exchanged (i.e., the target) is an investment company registered or required to be registered under the Investment Company Act.

As an alternative to Form F-9, Form F-10 can be used to register debt or preferred securities of a majority-owned Canadian subsidiary. If the majority-owned subsidiary (1) is incorporated or organized under the laws of Canada or a Canadian province or territory, and (2) is a foreign private issuer, it will be deemed to meet the reporting and public float requirements of Form F-10 if its parent: (1) meets all of the Form F-10 eligibility requirements, and (2) fully and unconditionally guarantees the securities being registered as to principal and interest (if debt securities) or as to liquidation preference, redemption price and dividends (if preferred securities). The debt or preferred securities being registered by the subsidiary may be convertible or exchangeable, but only for securities of the parent.

CHAPTER 5.

U.S. TRADING MARKETS AND LISTING

A. Introduction

The principal markets for trading securities in the United States, including those of foreign issuers, are the New York Stock Exchange LLC (“NYSE”), the NYSE Amex LLC (“NYSE Amex”) (formerly, the American Stock Exchange LLC (“Amex”))⁹¹ and the NASDAQ Stock Market LLC (“NASDAQ”). NASDAQ has three tiers: the NASDAQ Global Select Market, the NASDAQ Global Market (formerly known as the NASDAQ National Market) and the NASDAQ Capital Market (formerly known as the NASDAQ SmallCap Market). There are also: (i) other exchanges, called the “regional exchanges”; and (ii) electronic communications networks (“ECNs”) and other alternative trading systems (“ATSs”), which are SEC-approved non-exchange trading venues.

B. Hybrid Markets

The NYSE and NYSE Amex historically were auction markets, with open-outcry trading taking place on the exchange floor. Both the NYSE and NYSE Amex now follow hybrid market models to integrate the auction market with automated trading.

C. Over-the-Counter Market

The over-the-counter (“OTC”) market is the residual market where securities that are not listed on an exchange trade. It is not centralized; dealers execute OTC transactions over the phone or over the computer. Unlike the auction markets of the exchanges, in the OTC market there is no way for the orders of buyers and sellers to meet directly. In almost every OTC trade, there is a professional dealer (“market maker”) who makes markets by buying or selling securities for its own account. That is why the OTC market is known as a “dealer market.”

A security may trade in the OTC market through: (i) the OTC Bulletin Board (“OTCBB”), operated by the Financial Industry Regulatory Authority, Inc. (“FINRA”), as successor to the NASD; or (ii) OTCQX, OTCQB or the Pink Sheets, operated by Pink OTC Markets. The requirements that must be met for a security to be quoted on the OTCBB are provided in Appendix D.

D. Listing

1. Exchange Act Registration. Before a foreign issuer qualifies its securities for listing on an exchange, it must register those securities under Section 12 of the Exchange Act.

⁹¹ NYSE Euronext completed its acquisition of the Amex on October 1, 2008. Post merger, the Amex equities business was branded NYSE Alternext US. Subsequently, NYSE Alternext US was rebranded as NYSE Amex Equities (i.e., NYSE Amex).

2. Listing Requirements. An issuer that wants its securities to trade on a particular exchange must apply to that exchange for listing approval. Generally, an issuer seeking listing approval must meet numerical standards, financial reporting requirements and corporate governance policies, which vary by market. The listing standards for the NYSE, NYSE Amex, NYSE Arca, Inc. (“NYSE Arca”) (formerly known as the Pacific Exchange) and NASDAQ are provided in Appendices B and C.

CHAPTER 6.

PRIVATE PLACEMENTS

A. Introduction

Under the Securities Act, every offer, sale or delivery of a security must be covered by: (a) a registration statement under Section 5 of the Securities Act, or (b) an exemption from registration. The exemptions for “private placements” of securities are:

1. Section 4(2) of the Securities Act, which exempts from registration sales by an issuer not involving a public offering; and
2. Regulation D (i.e., Rules 501-508) under the Securities Act, which is a set of “safe harbor” provisions under which an issuer will be deemed to have satisfied the statutory exemption under Section 4(2) for private offerings or the statutory exemption under Section 3(b) of the Securities Act for small offerings. Regulation D is only available to issuers.

Issuers rely on these exemptions for a wide variety of transactions ranging from the initial sale of stock by a new company to billion dollar sales of equity or debt to hundreds of investors. These exemptions are also used for venture capital investments, acquisitions of closely held companies or for the sale of limited partnership or limited liability company interests in syndications and hedge funds.

B. Section 4(2): The Private Placement

Section 4(2) of the Securities Act provides an exemption from registration under Section 5 for “transactions by an issuer not involving any public offering.” The factors considered for a valid offering under Section 4(2) include the following:

1. Number and character of offerees (not just the purchasers).
 - (a) The number of offerees and sales are limited.
 - (b) The offerees should be sophisticated and able to bear the economic risk of their investment. Sophisticated investors include institutions – banks (sole investment discretion), key employees, individuals (with a relationship to issuer) and dealers.
2. Character of security offered. The nature of the offering and size of the blocks offered are relevant.
3. Availability of information. The offeree should be furnished with or have access to information comparable to that in a registration statement for the securities.
4. Manner of offering. The manner of offering must not involve any general advertising or general solicitation.

5. Absence of redistribution. Purchaser must purchase with “investment” intent, or at least without a “view to further distribution” in violation of the Securities Act.

6. Integration. Integration of the offered securities with other offerings by the issuer may occur if the offerings are made close in time to one another, resulting in the offerings being deemed one “public offering” and subject to Section 5 registration requirements. The factors considered in integrating offerings are:

- (a) the relationship of the offering to the time and purpose of other offerings;
- (b) whether the security offered is “different” from a security previously offered; and
- (c) the five factors listed in the Note to Rule 502(a) under the Securities Act, which are discussed below.

Rule 155 under the Securities Act addresses integration in the narrow circumstances of: (i) a private placement following an abandoned public offering, and (ii) a public offering following an abandoned private placement.

C. Regulation D (Rules 501-508)

Regulation D is a non-exclusive safe harbor from registration under Section 5 of the Securities Act. Therefore, if an offering fails to comply with the specific conditions of Regulation D, a Section 4(2) exemption from registration may still be available. Regulation D is available only to issuers.

Regulation D contains three different exemptions from registration. Rules 504 and 505 provide exemptions for certain small offerings under Section 3(b) of the Securities Act, limited to \$1 million and \$5 million, respectively, during any 12-month period. Rule 506 provides a safe harbor under Section 4(2) that does not limit the amount of the offering.

1. Rule 506

Rule 506 allows an issuer to sell an unlimited amount of its securities to an unlimited number of “accredited investors” (defined below) and to 35 non-accredited investors. The conditions to be met for an exemption under Rule 506 are:

(a) 35 Non-Accredited Investors. No more than 35 purchasers of the issue may be non-accredited investors, or the issuer must reasonably believe that to be the case.

(b) Sophistication of Non-Accredited Investors. Immediately before the sale, each purchaser who does not qualify as an “accredited investor,” either alone or with his “purchaser representative,” must be sophisticated, i.e., must have such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or the issuer must reasonably believe this to be the case. A “purchaser representative” must meet the requirements specified in Rule 501(h) under the Securities Act. Note that under

Regulation D only purchasers, not offerees, must meet the “sophistication test.” (Compare non-Regulation D offerings under Section 4(2).)

(c) Information. The information requirements vary depending on whether the offering is made to accredited investors only or also to non-accredited investors.

(i) Offerings to Accredited Investors. No specific information need be furnished to purchasers that are “accredited investors” even if other purchasers are not accredited investors. However, issuers are generally well advised to provide accredited investors with the same information that is provided to other purchasers in view of the anti-fraud provisions of the federal securities laws.

(ii) Offerings to Non-Accredited Investors. The issuer must provide a disclosure document to non-accredited investors a reasonable time before sale, but is not required to provide the disclosure document to accredited investors.

(A) Issuers Not Reporting Under the Exchange Act. Issuers that do not report under the Exchange Act (other than Regulation A eligible issuers) must provide non-financial information of the kind that is required in a prospectus of a Securities Act registration statement. The financial information that must be provided by non-reporting issuers varies depending on the size of the offering. Specifically:

(1) Non-Financial Information. The issuer must provide the information required in Part I of the form of registration statement that it would be permitted to file in a registered offering. If the issuer is eligible to use Regulation A, it may provide the information required in Part II of Form 1-A. Generally, this information describes the issuer, its business and the securities offered.

(2) Financial Information.

(I) For offerings up to \$2 million, the financial information required is the information required by Article 8 of Regulation S-X, except that only the issuer's balance sheet, which must be dated within 120 days of the start of the offering, must be audited.

(II) For offerings up to \$7.5 million, the financial statements required are those required in Form S-1 for smaller reporting companies. The balance sheet, and the income and cash flow statements, must be

audited. But, where an issuer (other than a limited partnership) cannot obtain audited financial statements without unreasonable effort or expense, then only the issuer's balance sheet, which must be dated within 120 days of the start of the offering, must be audited. Where the issuer is a limited partnership and cannot obtain the required financial statements without unreasonable effort or expense, it may furnish financial statements that have been prepared on the basis of Federal income tax requirements and examined and reported on in accordance with generally accepted auditing standards by an independent public or certified accountant.

(III) For offerings over \$7.5 million, the financial statements required are those required by the registration statement form that the issuer would be entitled to use. But, where an issuer (other than a limited partnership) cannot obtain audited financial statements without unreasonable effort or expense, then only the issuer's balance sheet, which must be dated within 120 days of the start of the offering, must be audited. Where the issuer is a limited partnership and cannot obtain the required financial statements without unreasonable effort or expense, it may furnish financial statements that have been prepared on the basis of Federal income tax requirements and examined and reported on in accordance with generally accepted auditing standards by an independent public or certified accountant.

(IV) Foreign Private Issuers. A foreign private issuer eligible to use Form 20-F must disclose the same kind of information as that required to be included in a registration statement filed under the Securities Act on the form it would be entitled to use. The financial statements need be audited only to the extent indicated above. All financial statements must be reconciled to U.S. GAAP (unless prepared in accordance with U.S. GAAP or IFRS as issued by the IASB).

(B) Exchange Act Reporting Issuers. Issuers subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act may use information contained in publicly-

available filings together with information about the offering and the use of proceeds from it. Specifically, if the issuer is subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act, at a reasonable time before the sale of securities the issuer must furnish to the purchaser the information specified in (I) or (II) below and, in either event, the information specified in (III) below:

(I) The issuer's annual report to shareholders for the most recent fiscal year, if that annual report meets the requirements of Rules 14a-3 or 14c-3 under the Exchange Act, the definitive proxy statement filed in connection with that annual report, and if requested by the purchaser in writing, a copy of the issuer's most recent Form 10-K under the Exchange Act.

(II) The information contained in an annual report on Form 10-K or in a registration statement on Form S-1 or S-11 under the Securities Act or on Form 10 under the Exchange Act, whichever filing is the most recent required to be filed.

(III) The information contained in any reports or documents required to be filed by the issuer under Sections 13(a), 14(a), 14(c), and 15(d) of the Exchange Act since the distribution or filing of the report or registration statement specified in (I) or (II) above, and a brief description of the securities being offered, the use of the proceeds from the offering and any material changes in the issuer's affairs that are not disclosed in the documents furnished.

If the issuer is a foreign private issuer, the issuer may provide, in lieu of the information specified in (I) or (II) above, the information contained in its most recent filing on Form 20-F or Form F-1.

- (C) Exhibits. Exhibits required to be filed with the SEC as part of a registration statement or report, other than an annual report to shareholders or parts of that report incorporated by reference in a Form 10-K report, need not be furnished to each purchaser that is not an accredited investor if the contents of material exhibits are identified and those exhibits are made available to a purchaser, upon his written request, a reasonable time before his purchase.

- (D) Information Provided to Accredited Investors. At a reasonable time before the sale of securities, the issuer must provide non-accredited investors with a list of all material written information provided to accredited investors and furnish non-accredited investors with any of the information requested by them.
 - (E) Questions. The issuer must make available to each purchaser, at a reasonable time before his purchase, the opportunity: (I) to ask questions and receive answers concerning the offering, and (II) to obtain any additional information that the issuer possesses or can acquire without unreasonable effort or expense that is necessary to verify the accuracy of information required to be delivered to the purchaser.
 - (F) Business Combinations and Exchange Offers. For business combinations or exchange offers, in addition to information required by Form S-4, the issuer must provide to each purchaser at the time the plan is submitted to security holders, or, with an exchange, during the course of the transaction and before sale, written information about any terms or arrangements of the proposed transactions that are materially different from those for all other security holders. For this requirement, an issuer that is not subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act may satisfy the requirements of Part I.B. or C. of Form S-4 by compliance with (A) above.
 - (G) Information about Limitations on Resale. At a reasonable time before the sale of securities, the issuer must advise non-accredited investors of the limitations on resale of the securities sold in the transaction. It is recommended: (I) that all purchasers be advised of the resale restrictions, and (II) that the securities contain restrictive legends in order to establish that the securities were not sold for redistribution to the public.
- (iii) Anti-Fraud Rule. The requirements of Rule 10b-5 under the Exchange Act (which are discussed below) apply to all private offerings.
 - (d) No General Advertising or General Solicitation. The securities must not be offered or sold by means of any form of general advertising or general solicitation. This includes, but is not limited to, the following:

- (A) any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio; and
- (B) any seminar or meeting whose attendees have been invited by any general solicitation or general advertising.

However, publication by an issuer of a notice under Rule 135c under the Securities Act (which provides a safe harbor for issuers' announcements of offerings not registered or required to be registered under the Securities Act) or filing with the SEC by an issuer of a notice of sales on Form D (discussed below) in which the issuer has made a good faith and reasonable attempt to comply with the requirements of the form, will not be deemed to constitute general solicitation or general advertising for Regulation D. Further, if the requirements of Rule 135e under the Securities Act (discussed in Chapter 3) are met, providing any journalist (U.S. or foreign) with access to press conferences held outside of the United States, to meetings with issuer or selling security holder representatives conducted outside of the United States, or to written press-related materials released outside the United States, at or in which a present or proposed offering of securities is discussed, will not be deemed to constitute general solicitation or general advertising for Regulation D.

(e) Limitations on Resale. Securities acquired in a Rule 506 or other Regulation D transaction (except for certain transactions under Rule 504) have the status of securities acquired in a transaction under Section 4(2) of the Securities Act, and are "restricted securities" as defined in Rule 144 under the Securities Act (which is discussed in Chapter 7). The issuer must exercise reasonable care to assure that the purchasers are not "underwriters" within the meaning of Section 2(a)(11) of the Securities Act. Reasonable care may be demonstrated by:

- (A) making reasonable inquiry to determine if the purchaser is acquiring the securities for himself or for other persons;
- (B) giving written disclosure to each purchaser before sale that the securities have not been registered under the Securities Act and, therefore, cannot be resold unless registered or sold under an exemption from registration; and
- (C) legending the securities (specifically, by placing a legend on the certificate or other document that evidences the securities stating that the securities have not been registered under the Securities Act and setting forth or referring to the restrictions on transferability and sale of the securities).

While taking these actions will establish the requisite reasonable care, it is not the exclusive method to demonstrate such care. Other actions by the issuer may satisfy this condition.

- (f) Accredited Investor.

An “accredited investor” includes, in relevant part:

- (i) any bank; savings and loan association; registered broker-dealer; insurance company; registered investment company; business development company; licensed small business investment company; employee plan with assets over \$5 million established and maintained by a state or certain state entities; employee benefit plan meeting certain requirements; private business development company;
- (ii) any director, executive officer or general partner of the issuer, or any director, executive officer or general partner of a general partner of that issuer;
- (iii) an entity (a corporation, business trust, partnership or limited liability company) with assets over \$5 million, not formed for the specific purpose of acquiring the securities offered;
- (iv) any trust with assets over \$5 million, not formed for the specific purpose of acquiring the securities offered, whose purchase is directed by a sophisticated person;
- (v) any natural person with a net worth (together with its spouse) at the time of purchase of more than \$1 million excluding the value of the primary residence of such natural person (net of related indebtedness up to the fair market value of the residence);
- (vi) any natural person with income greater than \$200,000 in each of the last two years, or with income together with its spouse in excess of \$300,000 in each of those years, and with a reasonable expectation of reaching the same income level in the current year; and
- (vii) any entity in which all of the equity owners are accredited investors.

2. Rule 505

Rule 505 permits an issuer (other than an investment company) to sell securities with an aggregate offering price of up to \$5 million in a 12-month period. However, the \$5 million limit is reduced by any other sales made in reliance on exemptions under Section 3(b) of the Securities Act (e.g., Rule 504).

Conditions to be met:

(a) No more than 35 purchasers of the offering may be non-accredited investors, or the issuer must reasonably believe that to be the case. Unlike Rule 506, there is no condition of “sophistication,” i.e., knowledge and experience, of the non-accredited purchasers.

(b) The issuer must not be a “bad-boy,” i.e., disqualified under the provisions of Rule 262 under the Securities Act (relating to various regulatory or criminal proceedings concerning the issuer or certain related persons).

(c) The same conditions as under Rule 506 apply to information provided to purchasers, the absence of general advertising or general solicitation, and limitations on resale.

3. Rule 504

Rule 504 permits an issuer not subject to Exchange Act reporting requirements to sell securities with an aggregate offering price of up to \$1 million in a 12-month period. However:

(a) The \$1 million limit is reduced by any other sales made in reliance on exemptions under Section 3(b) of the Securities Act (e.g., Rule 505).

(b) Investment companies and “blind pool” companies are excluded, i.e., they cannot use Rule 504.

There are no specific requirements for information provided to offerees. The same conditions as under Rule 506 apply to the absence of general advertising or general solicitation and limitations on resale unless the offering is registered in a state requiring delivery of an offering document (and such delivery is made to all purchasers) or made only under state exemptions from registration permitting general advertising and general solicitation where sales are made solely to “accredited investors.”

4. Additional Regulation D Conditions. For each exemption under Regulation D, there are general conditions that must be met in addition to the specific conditions described above.

(a) Integration. An offering by the issuer that occurs around the time of a Regulation D offering may be integrated with it in some circumstances. If the two offerings are integrated, all the sales in both offerings would be counted together in determining whether the conditions of a Regulation D offering have been met. Regulation D provides two tests for determining whether the two offerings would be integrated:

- (i) Six Months Test. Offers and sales made more than six months before the start, and more than six months after the completion, of a Regulation D offering will not be considered part of that Regulation D offering.

- (ii) Five Factors Test. Even if offers and sales of another offering occur within six months of a Regulation D offering, the issuer may avoid integration based on the five factors test. The following factors are considered in determining whether offers and sales should be integrated for purposes of a Regulation D exemption:
 - (A) whether the sales are part of a single plan of financing;
 - (B) whether the sales involve issuance of the same class of securities;
 - (C) whether the sales have been made at or about the same time;
 - (D) whether the same type of consideration is being received; and
 - (E) whether the sales are made for the same general purpose.

(b) Filing of Notice of Sales. A notice of sales on Form D must be filed within 15 calendar days after the first sale of securities in the Regulation D offering (unless the end of that period falls on a Saturday, Sunday, or holiday, in which case the due date would be the first business day following). Failure to make a timely filing of Form D after sales in reliance on a Regulation D offering does not render the exemption unavailable for that offering. However, Rule 507 provides that an issuer may be disqualified from using a Regulation D exemption in the future if it, any of its predecessors or affiliates has ever been enjoined for failure to comply with the notice-filing requirement of Rule 503, an unlikely occurrence.

5. Substantial Compliance with Regulation D. Rule 508 provides that a failure to comply with a term, condition or requirement of Rule 504, 505 or 506 will not result in the loss of the exemption from registration for an offer or sale to a particular individual or entity, if the person relying on the exemption shows that:

- (a) the failure to comply did not pertain to a term, condition or requirement directly intended to protect that particular individual or entity;
- (b) the failure to comply was insignificant to the offering as a whole; and
- (c) a good faith and reasonable attempt was made to comply with all applicable terms, conditions and requirements of the particular exemption's provisions.

Certain conditions are never insignificant to the offering as a whole. These include the prohibition on general advertising or general solicitation, the dollar thresholds in Rules 504 and 505 and the limitations on the number of non-accredited purchasers.

D. Liability In Private Placements

1. Significance of Compliance. Non-compliance with Section 4(2) for a sale results in a violation of Section 5 of the Securities Act, and the purchaser can rescind the sale (i.e., "put"

the security to the issuer or the agent/purchaser). Additionally, enforcement action may be taken.

2. Section 12(a)(2) of the Securities Act does not apply to private placements.

3. Rule 10b-5 under the Exchange Act:

(a) Rule 10b-5 provides liability for material misstatements or omissions in connection with the purchase or sale of a security. Under Rule 10b-5, a plaintiff must prove “scienter” (i.e., intent to defraud, knowing misconduct or, possibly, reckless conduct).

(b) Rule 10b-5 requires a broker-dealer who recommends a security to a customer to have a reasonable basis for the recommendation, which in turn requires a reasonable investigation of the issuer. The sufficiency of any such investigation depends on the facts and circumstances of the transaction.

4. Section 17(a)(2) of the Securities Act. It is unlikely that Section 17(a)(2) provides a private cause of action.

E. Regulation FD

The SEC’s rules against “selective disclosure,” contained in Regulation FD, provide that whenever a U.S. public company, or a person acting on its behalf, discloses material non-public information about the issuer or its securities to any securities market professional, or to any holder of the issuer’s securities under circumstances in which it is reasonably foreseeable that the holder will purchase or sell the issuer’s securities on the basis of the information, then the issuer must make public disclosure of that information, unless the recipient expressly agrees to maintain the information in confidence or owes a duty of trust or confidence to the issuer. Regulation FD does not provide an exemption for communications made in unregistered offerings, such as private placements. Thus, all disclosures of material non-public information made in private placements will trigger Regulation FD’s “public disclosure” requirement, unless all recipients of the information expressly agree not to disclose or trade on the basis of the information. The release adopting Regulation FD makes clear that such public disclosure is appropriate even if it calls into question the private placement or other exemption from registration upon which an issuer is relying, although in most cases it should be possible to disclose the material information without also publicly disclosing offering details that would jeopardize the exemption. (Where the fact of the offering itself may be considered material, Rule 135c under the Securities Act would permit a Form 8-K filing containing basic information about the terms of the securities offered, the size and timing of the offering and a brief statement of its purpose, without naming the underwriters or placement agents.)

The SEC has stated that, while Regulation FD does not apply to foreign issuers, those issuers in their disclosure practices remain subject to liability for conduct that violates, and meets the jurisdictional requirements of, the anti-fraud provisions of the U.S. federal securities laws. Accordingly, even though Regulation FD does not apply to foreign issuers, many foreign private issuers choose to comply with the terms of Regulation FD.

F. State “Blue Sky” Laws

Any private placement must be qualified at both the state and federal levels. The patchwork of differing state securities laws can make compliance complex. However, state securities laws applicable to Rule 506 offerings that conflict with federal law have generally been preempted. Nevertheless, even for Rule 506 offerings, states may require notice filings and payment of fees.

CHAPTER 7.

RESALES OF SECURITIES

A. Introduction

Under the Securities Act, every offer or sale of a security must be covered by a registration statement under Section 5 of the Securities Act or an exemption from registration. Regulation D was intended to provide certainty for the issuer's exemption, but it did not provide an exemption for resales of securities acquired by investors in a private placement.

Securities issued in a private placement are characterized as “restricted securities” and can be resold in the United States under Rule 144, Rule 145, Section 4(1½), Rule 144A, Regulation A, or a registration statement or outside the United States under Regulation S.

B. Statutory Framework

Section 5(c) of the Securities Act makes it unlawful for any person, directly or indirectly, to offer securities using the “jurisdictional means” unless a registration statement has been filed for those securities. Section 5(a) of the Securities Act makes it unlawful for any person, directly or indirectly, to sell or deliver securities using the “jurisdictional means” unless a registration statement is in effect for those securities.

1. Definitions

(a) Section 2(a)(2): “person” includes individuals and entities.

(b) Section 5: “jurisdictional means” means the U.S. mails, and also, the instrumentalities of “interstate commerce.” Under Section 2(a)(7), “interstate commerce” means “commerce . . . among the several States or . . . between any foreign country and any State”

(c) Section 2(a)(3): “offer” includes “every attempt or offer to dispose of, or solicitation of an offer to buy, a security . . . for value.”

(d) Section 2(a)(3): “sale” includes “every . . . disposition of a security . . . for value.”

(e) Section 2(a)(1): “security” – this definition is discussed in Chapter 2.

2. Exemptions

(a) Section 3 of the Securities Act lists various “exempt securities.” The registration requirement of Section 5 does not apply to:

(i) Section 3(a)(2): U.S. government and agency securities, state and municipal securities, banks’ securities.

- (ii) Section 3(a)(3): commercial paper with a maturity not exceeding nine months.
- (iii) Section 3(a)(4): securities of religious, benevolent, educational, fraternal, charitable and reformatory organizations.

(b) Section 3 also lists securities that are “exempt” but only for particular transactions. The registration requirement of Section 5 does not apply to:

- (i) Section 3(a)(9): securities exchanged by the issuer with its existing security holders exclusively, where no remuneration is paid for soliciting the exchange.
- (ii) Section 3(a)(10): securities that are issued in exchange for one or more bona fide outstanding securities, claims or property interests, or partly in such exchange and partly for cash, where the issuance is approved by a court or by a federal or state official expressly authorized to approve the issuance, after an open hearing on the fairness of the terms and conditions of the issuance.
- (iii) Section 3(a)(11): securities that are part of intrastate offerings (specifically, securities that are part of issues offered and sold only to persons resident within a single State or Territory, where the issuer of the securities is a person resident and doing business within or, if a corporation, incorporated by and doing business within, that State or Territory).
- (iv) Section 3(b): securities that are part of issues not exceeding \$5 million, per SEC rule or regulation, e.g., Regulation A, Rule 504 or Rule 505.

(c) Section 4 lists exempt transactions. The registration requirement of Section 5 does not apply to:

- (i) Section 4(1): transactions by any person other than an issuer, underwriter or dealer.
- (ii) Section 4(1½): private resales. This section is not in the statute. See D. below.
- (iii) Section 4(2): transactions by an issuer not involving any public offering.
- (iv) Section 4(3): transactions by a dealer (including an underwriter no longer acting as such for the security involved in the transaction), except: (A) transactions within 40 days after the first date on which the security was bona fide offered to the public by the issuer or by or through an underwriter; (B) transactions in a security as to

which a registration statement has been filed taking place within 40 days after effectiveness of the registration statement or within 40 days after the first date on which the security was bona fide offered to the public by the issuer or by or through an underwriter after effectiveness of the registration statement, whichever is later (or within such shorter period as the SEC may specify by rule, regulation or order); and (C) transactions in securities constituting all or part of an unsold allotment to that dealer as a participant in the distribution of those securities by the issuer or by or through an underwriter.

For transactions referred to in (B) above, if securities of the issuer have not previously been sold under an earlier effective registration statement (generally, for an issuer's IPO in the United States), the applicable period, instead of 40 days, will be 90 days (or such shorter period as the SEC may specify by rule, regulation or order.) The SEC, via Rule 174 under the Securities Act, has shortened the 40 (or 90) day period for transactions referred to in (B) above.

- (v) Section 4(4): brokers' transactions executed upon customers' orders on any exchange or in the over-the-counter market, but not the solicitation of such orders.
- (vi) Section 4(5): transactions involving offers or sales by an issuer solely to one or more accredited investors, if: the aggregate offering price of an issue of securities offered in reliance on this exemption does not exceed \$5 million, there is no advertising or public solicitation in connection with the transaction by the issuer or anyone acting on the issuer's behalf, and the issuer files Form D with the SEC.

3. Operation of Section 4

The operation of Section 4 is intricate:

(a) Section 4(1) exempts all transactions by every person other than an issuer, underwriter or dealer.

(b) Section 4(3) exempts all dealer transactions, except: (1) transactions within 40 days of public offering of the security; (2) transactions within 40 (or 90) days after the effectiveness of, or within 40 (or 90) days after the security was first offered to the public after the effectiveness of, a registration statement (or within such shorter period as is prescribed by SEC rule – see Rule 174); and (3) offers and sales of unsold allotments as a participant in a distribution.

(c) Read together, Sections 4(1) and 4(3) exempt all transactions by anyone other than: (i) the issuer (the term “issuer,” in this usage, does NOT include its control persons),

(ii) an underwriter, or (iii) a dealer trading (as broker or as dealer) in unsold allotments or within 40 (or 90) days after a public offering of the security.

Taken together, these two exemptions permit all trades in the secondary markets.

(d) The scope of the term “issuer” is relatively clear. As in corporate law, there are certain alter ego circumstances in which associated persons may be included in the term “issuer.” Similarly, the meaning of “dealer” is clear; the only question here is, what about dealer transactions before the first public offering?

4. The “Statutory Underwriter” Problem

(a) The problem is the scope of the term “underwriter.” “Underwriter” is defined in Section 2(a)(11) of the Securities Act as “any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking” As used in this definition, the term “issuer” includes, “in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.”

This definition gives rise to the following questions: If the prospective reseller has bought the security from its issuer (or from one of the issuer’s controlling persons), did that prospective seller buy with a view to “distribution” – i.e., with a view to offering indiscriminately to members of the public? Or did that prospective seller offer or sell for the issuer (or for one of the issuer’s controlling persons) in connection with an offering indiscriminately to members of the public? Or did that prospective seller have a participation in any such scheme?

(b) Under these definitions, three types of transactions may be found to involve an “underwriter” and, therefore, require registration.

- (i) Resales of securities acquired in a private placement. If a person buys securities from an issuer in a private placement and resells them to the public, his conduct evidences a purchase “with a view to . . . distribution.” So, he is an “underwriter” and cannot avail himself of Section 4(1).
- (ii) Sales of securities by controlling persons (sales of “restricted securities” and securities purchased in the open market which were not held for a significant period of time).

If a broker acts for a company’s controlling person in the sale of shares of the company’s stock in the open market, the broker is offering and selling for a controlling person of the issuer in connection with a “distribution.” So, the broker is an “underwriter” (whether or not it is a non-exempt dealer) and cannot avail itself of Section 4(1) or Section 4(3). (However, the Section 4(1) exemption would be available to the control person selling non-restricted securities who sold his securities directly to the public without any intermediary.)

- (iii) Sales by a broker or anyone else on behalf of a controlling person.
See (ii) above.

C. Rule 144

1. Introduction

In response to the uncertainties described above, the SEC adopted Rule 144 under the Securities Act (which is not the same as Rule 144A under the Securities Act, discussed in E. below). Rule 144 provides to security holders a safe harbor for relying on the Section 4(1) exemption for resales of securities. In other words, Rule 144 provides objective criteria for permissible resales to the public of unregistered and control securities without registration. Rule 144 provides an exemption from registration for: (a) the resale of “restricted securities” (defined below); (b) the resale of all securities (i.e., restricted and non-restricted or “control” securities) of an issuer held by “affiliates” of the issuer (i.e., held by “control persons”); and (c) those who sell securities for the account of an affiliate.

(a) Definitions

Two definitions under Rule 144 are particularly important:

- (i) Affiliate. An “affiliate” of the issuer is a person, such as a director or large shareholder, in a relationship of control with the issuer. Specifically: (A) under Rule 144, an “affiliate” of an issuer is any person who directly or indirectly controls, is controlled by, or is under common control with, the issuer; and (B) “control” means the power to direct the management and policies of the issuer, whether through the ownership of voting securities, by contract, or otherwise.
- (ii) Restricted Securities. “Restricted securities” are securities acquired in unregistered, private sales from the issuer or from an affiliate of the issuer. Investors typically receive restricted securities through private placement offerings, Regulation D offerings, employee stock benefit plans, as compensation for professional services, or in exchange for providing “seed money” or start-up capital to the company. Rule 144(a)(3) identifies what sales produce restricted securities. Specifically, under Rule 144(a)(3), “restricted securities” are: (1) securities acquired directly or indirectly from an issuer or its affiliate in a transaction or chain of transactions not involving any public offering; (2) securities acquired from the issuer that are subject to the resale limitations of Regulation D or Rule 701(g) under the Securities Act (for certain compensation plans); (3) securities acquired in a transaction or chain of transactions meeting the requirements of Rule 144A; (4) securities acquired from the issuer in a transaction subject to the conditions of Regulation CE (i.e., Rule 1001) under the Securities

Act (for certain securities issuances exempt under California law); (5) equity securities of U.S. issuers acquired in a transaction or chain of transactions subject to the conditions of Rule 901 or Rule 903 of Regulation S; (6) securities acquired in a rights offering made under Rule 801 under the Securities Act to the same extent and proportion that the securities held by the security holder of the class with respect to which the rights offering was made were, as of the record date for the rights offering, “restricted securities”; (7) securities acquired in an exchange offer or business combination made under Rule 802 under the Securities Act to the same extent and proportion that the securities that were tendered or exchanged were “restricted securities”; and (8) securities acquired from the issuer in a transaction subject to an exemption under Section 4(5) of the Securities Act.

(b) Structure of Rule 144

When adopting Rule 144, the SEC stated that three factors were important in determining whether a person is deemed not to be engaged in a distribution requiring registration:

- (i) the purpose and policy of the Securities Act is to protect investors and requires that there be adequate current information concerning the issuer;
- (ii) a holding period before resale is essential to assure that those who buy under a private placement exemption have assumed the economic risks of the investment and are not acting as conduits for sale to the public of unregistered securities on behalf of the issuer; and
- (iii) the impact of the particular transactions on the trading market.

Based on these principles, the specific conditions of the Rule were developed.

2. A Person Meeting the Conditions of Rule 144 Is Not an Underwriter

Rule 144 provides a safe harbor from the Section 2(a)(11) definition of “underwriter.” A person meeting the conditions of Rule 144 is deemed not to be engaged in a distribution of the securities and, therefore, not an underwriter of the securities for Section 2(a)(11). Therefore, that person is deemed not to be an underwriter when determining whether the sale is eligible for the Section 4(1) exemption from registration under Section 5 of the Securities Act for “transactions by any person other than an issuer, underwriter, or dealer.” If a sale complies with the conditions of Rule 144: (a) any affiliate of the issuer (“affiliate”) or other person who sells restricted securities for his own account will be deemed not to be engaged in a distribution and, therefore, not an underwriter for that transaction; (b) any person who sells restricted or other securities for the account of an affiliate will be deemed not to be engaged in a distribution and, therefore, not an underwriter for that transaction; and (c) the purchaser in the transaction will receive securities that are not restricted securities.

3. Summary of Rule 144

The following summarizes Rule 144:

(a) For Restricted Securities of Reporting Issuers

- | | |
|---|--|
| (i) Non-Affiliate (and Has Not Been an Affiliate During the Prior Three Months) | <i>During six-month holding period</i> - no resales under Rule 144 permitted.

<i>After six-month holding period but before one year</i> - unlimited public resales under Rule 144 permitted, except that the current public information requirement still applies.

<i>After one-year holding period</i> - unlimited public resales under Rule 144 permitted; need not comply with any Rule 144 requirements. |
| (ii) Affiliate or Person Selling on Behalf of an Affiliate | <i>During six-month holding period</i> – no resales under Rule 144 permitted.

<i>After six-month holding period</i> - may resell in accordance with all Rule 144 requirements, including: <ul style="list-style-type: none">• current public information,• volume limitations,• manner of sale requirements for equity securities, and filing of Form 144. |

(b) For Restricted Securities of Non-Reporting Issuers

- | | |
|---|---|
| (i) Non-Affiliate (and Has Not Been an Affiliate During the Prior Three Months) | <i>During one-year holding period</i> - no resales under Rule 144 permitted.

<i>After one-year holding period</i> - unlimited public resales under Rule 144 permitted; need not comply with any Rule 144 requirements. |
| (ii) Affiliate or Person Selling on Behalf of an Affiliate | <i>During one-year holding period</i> - no resales under Rule 144 permitted.

<i>After one-year holding period</i> - may |

resell in accordance with all Rule 144 requirements, including:

- current public information,
- volume limitations,
- manner of sale requirements for equity securities, and
- filing of Form 144.

(c) For Non-Restricted Securities

The holding period only applies to restricted securities. Because securities acquired in the public market are not restricted, there is no holding period for an affiliate who purchases securities of the issuer in the marketplace. But the resale of an affiliate's shares is subject to the other conditions of Rule 144.

(d) Conditions of Rule 144

(i) Current Public Information

Adequate current public information about the issuer must be available. How this requirement is satisfied depends on whether the issuer is a reporting issuer or a non-reporting issuer. To qualify as a “reporting issuer” for Rule 144, the issuer must be, and have been for at least 90 days immediately before the sale, subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act.

For a reporting issuer, the “current public information” requirement is met if the issuer: (A) has filed all required reports during the 12 months preceding the sale (or for whatever shorter period it was required to file reports), other than Form 8-K reports; and (B) has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted under Rule 405 of Regulation S-T, during the 12 months preceding the sale (or for whatever shorter period it was required to submit and post such files).

For a non-reporting issuer (other than an insurance company), the “current public information” requirement is met if specified portions of the information required by Rule 15c2-11 under the Exchange Act is publicly available. This includes information on the nature of the issuer’s business, members of its board of directors, its most recent profit and loss and retained earnings statements, and comparable financial information for the last two fiscal years. For a non-reporting issuer that is an insurance company, the current public information requirement is met if the information specified in Section 12(g)(2)(G)(i) of the Exchange Act is publicly available.

(ii) Holding Period for Restricted Securities

A minimum of six months or one year, as applicable, must elapse between: (A) the later of the date the securities were acquired from the issuer or from an affiliate of the issuer, and (B) any resale of the securities under the Rule by either the initial holder of the securities or any subsequent holder. The Rule permits a holder of restricted securities to tack his holding period to the holding periods of prior unaffiliated holders for purposes of meeting the holding period. However, the holding period does not begin until the purchase price is paid in full by the initial holder.

In certain instances, the Rule permits the seller to add his holding period to that of a predecessor holder or to his own holding period for other securities.

Pledged Securities: Securities that are bona-fide pledged by an affiliate of the issuer when sold by the pledgee, or by a purchaser, after a default in the obligation secured by the pledge, will be deemed to have been acquired when they were acquired by the pledgor, except that if the securities were pledged without recourse they will be deemed to have been acquired by the pledgee at the time of the pledge or by the purchaser at the time of purchase.

Gifts of Securities: Securities acquired from an affiliate of the issuer by gift will be deemed to have been acquired by the donee when they were acquired by the donor.

Trusts: Where a trust settlor is an affiliate of the issuer, securities acquired from the settlor by the trust, or acquired from the trust by the beneficiaries of it, will be deemed to have been acquired when the securities were acquired by the settlor.

Estates: Where a deceased person was an affiliate of the issuer, securities held by the estate of that person or acquired from that estate by the estate beneficiaries will be deemed to have been acquired when they were acquired by the deceased person, except that no holding period is required if the estate is not an affiliate of the issuer or if the securities are sold by a beneficiary of the estate who is not an affiliate of the issuer. (While there is no holding period or amount limitation for estates and estate beneficiaries that are not affiliates of the issuer, the current public information and notice of proposed sale requirements apply to securities sold by such persons in reliance on Rule 144.)

Stock dividends, stock splits, and stock acquired in recapitalizations, conversions, exchanges or contingent issuances of securities may be tacked. Stock acquired in conversions and exchanges may be tacked even if the securities surrendered were not convertible or exchangeable by their terms. Rule 144 states that if: (1) the original securities do not permit cashless conversion or exchange by their terms, (2) the parties amend the original securities to allow for cashless conversion or exchange, and (3) the security holder provides consideration, other than solely securities of the issuer, for that amendment, then the newly acquired securities will be deemed to have been acquired on the date of the amendment of the original securities (not the date the securities were originally purchased) as long as, in the

conversion or exchange, the securities to be sold were acquired from the issuer solely in exchange for other securities of the same issuer.

Additionally, security holders may tack the Rule 144 holding period for securities acquired in transactions made solely to form a holding company.

Specifically, Rule 144 permits the tacking of the holding period of the restricted securities of the predecessor company to the holding period of the restricted securities of the holding company received in the reorganization if three conditions are met: (1) the newly formed holding company's securities were issued solely in exchange for the securities of the predecessor company as part of a reorganization of the predecessor company into a holding company structure; (2) security holders received securities of the same class, evidencing the same proportional interest in the holding company as they held in the predecessor company, and the rights and interests of the security holders are substantially the same as those they possessed as security holders of the predecessor company's securities; and (3) immediately following the transaction, the holding company has no significant assets other than securities of the predecessor company and its existing subsidiaries, and has substantially the same assets and liabilities on a consolidated basis as the predecessor company had before the transaction.

Additional securities purchased from the issuer do not affect the holding period of previously purchased securities of the same class.

Cashless Exercise of Options and Warrants: Upon a cashless exercise of options or warrants, the newly acquired underlying securities are deemed to have been acquired when the corresponding options or warrants were acquired, even if the options or warrants originally did not provide for cashless exercise by their terms. Rule 144 states that if (1) the original options or warrants do not permit cashless exercise, and (2) the security holder provides consideration, other than solely securities of the issuer, to amend the options or warrants to allow for cashless exercise, then the newly acquired underlying securities would be deemed to have been acquired on the date that the original options or warrants were so amended (similar to the treatment of conversions and exchanges above).

Additionally, the grant of certain options or warrants that are not purchased for cash or property (e.g., employee stock options) does not create an investment risk for the security holder. Consequently the holder cannot tack the holding period for the options or warrants to the holding period for the securities received upon exercise of the options or warrants. Therefore, the security holder would be deemed to have acquired the underlying securities on the date the option or warrant was exercised (not the date granted), so long as the full purchase price for the newly acquired securities has been paid at the time of exercise.

(iii) Limitation on Amount of Securities Sold

- (A) If securities are sold for the account of an affiliate of the issuer, regardless of whether those securities are restricted, the amount of securities sold, together with all sales of securities of the same class sold for the account of that person within the preceding three months, may not exceed the greatest of: (1) 1% of the shares or other units of the

class outstanding as shown by the most recent report or statement published by the issuer; (2) the average weekly reported trading volume in such securities on all national securities exchanges in the United States and/or reported through an automated quotation system in the United States during the four calendar weeks preceding the filing of a notice of proposed sale on Form 144 (or, if no such notice is required, the date the broker receives the order to execute the transaction or the date the transaction is executed directly with a market maker); or (3) the average weekly trading volume in such securities reported under an “effective transaction reporting plan” or an “effective national market system plan,” as those terms are defined in Rule 600 of Regulation NMS (i.e., reported on the consolidated tape), during the four-week period described in (2) above. Over-the-counter stocks, including those quoted on the OTC Bulletin Board and the Pink Sheets, can only be sold using the 1% measurement.

- (B) Rule 144 provides an alternative volume limitation for the resale of debt securities. It permits the resale of debt securities that does not exceed 10% of a tranche (or class for non-participatory preferred stock), when aggregated with all sales of securities of the same tranche (or class for non-participatory preferred stock) sold by the security holder within three months. Specifically, if the securities sold are debt securities, then the amount of debt securities sold for the account of an affiliate of the issuer, regardless of whether those securities are restricted, may not exceed the greater of: (1) the volume limitation set forth in (A) above; or (2) 10% of the principal amount of the tranche (or class for non-participatory preferred stock) attributable to the securities sold, when aggregated with all sales of securities of the same tranche (or class for non-participatory preferred stock) sold for the account of that person within the preceding three months.
- (C) Certain sales must be aggregated for purposes of these quantity limitations, particularly if tacking is permitted.

(iv) Manner of Sale

For affiliates, sales of equity securities under Rule 144 must be made in: (A) “brokers’ transactions” within the meaning of Section 4(4) of the Securities Act; (B) transactions directly with a “market maker” as defined in Section 3(a)(38) of the Exchange Act; or (C) “riskless principal transactions” (as defined in Rule 144) where: (1) the offsetting trades must be executed at the same price (exclusive of an explicitly disclosed markup or

markdown, commission equivalent or other fee); (2) the transaction is permitted to be reported as riskless under the rules of a self-regulatory organization; and (3) the requirements of Rule 144(g)(2) (applicable to any markup or markdown, commission equivalent or other fee), Rule 144(g)(3) and Rule 144(g)(4) (see below) are met. Additionally, an affiliate selling equity securities under Rule 144 must not: (A) solicit buy orders, or (B) make any payment in connection with the offer or sale of the securities to any person other than the broker or dealer who executes the sell order.

“Brokers’ transactions” include transactions in which the broker: (A) merely executes the sell order as agent; (B) receives no more than the usual and customary broker’s commission (Rule 144(g)(2)); (C) generally, does not solicit buy orders (Rule 144(g)(3)); and (D) makes reasonable inquiry into the seller and the circumstances of the proposed sale (Rule 144(g)(4)).

A “market maker” is defined in Section 3(a)(38) as “any specialist permitted to act as a dealer, any dealer acting in the capacity of block positioner, and any dealer who, with respect to a security, holds himself out (by entering quotations in an inter-dealer communications system or otherwise) as being willing to buy and sell such security for his own account on a regular or continuous basis.”

For Rule 144, a “riskless principal transaction” is “a principal transaction where, after having received from a customer an order to buy, a broker or dealer purchases the security as principal in the market to satisfy the order to buy or, after having received from a customer an order to sell, sells the security as principal to the market to satisfy the order to sell.”

The “manner of sale” requirement does not apply to: (A) resales of debt securities (including non-participatory preferred stock and asset-backed securities) held by affiliates of the issuer; or (B) securities sold for the account of the estate of a deceased person or for the account of a beneficiary of such estate provided the estate or estate beneficiary is not an affiliate of the issuer.

(v) Notice of Proposed Sale

If the seller is an affiliate, it must file a Form 144 with the SEC and, if the securities are admitted to trading on any national securities exchange, the principal exchange on which the securities are traded. However, no notice is required for sales during any three-month period that do not exceed 5,000 shares (or other units) or \$50,000.

(vi) Bona Fide Intention to Sell

The seller filing the Form 144 notice must have a bona fide intention to sell the securities within a reasonable time after the filing of the notice. The sale must take place within three months of filing the Form and, if the securities have not been sold, an amended notice must be filed.

4. Documentation to Establish the Exemption

Although not required by the Rule, practitioners generally obtain a standard set of papers to document compliance with the Rule. These papers include: (a) a seller's representation letter discussing: whether such person is an affiliate, the filing of a Form 144 notice with the SEC, and the manner in which the securities are to be sold; (b) a broker's representation letter; and (c) a completed Form 144, if required.

5. Non-exclusivity of Rule 144 – Reselling Restricted Securities Outside Rule 144

Rule 144 is not exclusive and sales of restricted securities may be made under other exemptions from registration or by registration.

D. Section 4(1½) – Private Resales

Private resales of restricted securities outside Rule 144 (i.e., outside the public markets during the one-year period) are fairly common. Generally, the SEC has not objected when one private placement investor holding restricted securities privately negotiated and sold those securities to another, if the buyer agreed to hold the securities subject to the same restrictions as those that bind the seller. These private resales are structured similar to a Section 4(2) private placement, but Section 4(2) does not apply because by its terms it applies only to transactions by an issuer. The statutory exemption for these private resales is Section 4(1), which exempts transactions by any person other than an issuer, underwriter or dealer. To use the Section 4(1) exemption, the person reselling the privately placed securities must avoid being characterized as an “underwriter,” i.e., the seller must not have: (a) purchased the securities from the issuer in the private placement “with a view to . . . [their] distribution,” or (b) offered or sold the securities “for an issuer in connection with, the distribution of any security.”

The private bar reasoned that if there is no “distribution,” then the seller could not be an “underwriter” and the seller would have a valid Section 4(1) exemption. Consequently, for limited resales from one private placement investor to another, to avoid a distribution, the private bar developed fairly standardized procedures similar to those used to ensure the availability of the Section 4(2) exemption and, concomitantly, the absence of a public offering or distribution. This bar-created exemption for private resales based on Section 4(1) but with Section 4(2) procedures is called Section 4(1½). Non-underwriter status is established by: (a) no general advertising or general solicitation; (b) resale restrictions, such as “investment” or “non-distribution” letters (containing basically the same representations and agreements as those provided by the original purchasers); and (c) requirements for legal opinions. Restrictive legends placed on the certificates and stop transfer procedures remain in place from the initial private placement.

In effect, use of the Section 4(1½) restrictions keeps the privately placed securities outside the public markets (unless registered), until they can be sold under Rule 144.

E. Rule 144A – Resales to Qualified Institutional Buyers

Rule 144A provides a non-exclusive safe harbor exemption from registration under Section 4(1) of the Securities Act for resales of certain restricted securities by persons other than

the issuer (and Section 4(3) for dealers) to qualified institutional buyers (“QIBs”). Rule 144A, in effect, permits “underwritten private placements.”

1. Conceptual Basis

Certain institutions are conclusively assumed to be sophisticated and thus not in need of the protection of the registration requirement of the federal securities laws. Consequently, sales to such institutions are deemed not to constitute a public offering, and the offers and sales are not subject to the registration requirement of Section 5 of the Securities Act.

2. Regulatory Scheme

The Rule 144A regulatory scheme for sales of 144A securities is as follows: issuer to dealer, the transaction is exempt under Section 4(2) (as a private placement); dealer to QIB, the transaction is exempt under Rule 144A by Section 4(3) (the dealer exemption); QIB back to dealer for continuing resales to other QIBs, the transaction is exempt under Rule 144A by Section 4(1) (the exemption for sales by other than an issuer, underwriter or dealer).

Under Preliminary Note 7 to Rule 144A, a purchase by a dealer from the issuer with a view to resale under Rule 144A will not affect the availability of the Section 4(2) private placement exemption, i.e., the dealer will not be classified as an “underwriter” by virtue of its intention to make immediate resales to QIBs.

3. Conditions

The conditions of Rule 144A are as follows:

(a) Qualified Institutional Buyers. The seller (and any person acting on its behalf) must reasonably believe that the securities are being offered or sold only to QIBs. A “QIB” is any specified entity acting for its own account or the accounts of other QIBs that, in the aggregate, owns and invests, on a discretionary basis, at least \$100 million in securities of issuers unrelated to the entity. Examples of QIBs include: insurance companies, registered investment companies, business development companies (as defined in the Investment Company Act or the Advisers Act), licensed small business investment companies, state and ERISA employee benefit plans, trust funds whose trustee is a bank or trust company and whose participants are exclusively state and ERISA employee benefit plans (except trust funds that include as participants individual retirement accounts or H.R. 10 plans), corporations, partnerships, registered investment advisers, U.S. and foreign banks, and U.S. and foreign savings and loan associations. In addition to meeting the \$100 million asset test, a bank or savings and loan association must have an audited net worth of at least \$25 million as demonstrated in its latest annual financial statements, as of a date not more than 16 months before the date of sale (18 months for a foreign bank or foreign savings and loan association).

A registered broker-dealer is a QIB if: (i) it owns and invests, on a discretionary basis, at least \$10 million in securities of issuers that are unrelated to it; or (ii) it acts as a riskless principal for an identified QIB. (For Rule 144A, a “riskless principal transaction” is a transaction in which a dealer buys a security from any person and makes a simultaneous offsetting sale of such security to a QIB, including another dealer acting as riskless

principal for a QIB.) A registered broker-dealer may also act as agent, on a non-discretionary basis, in a transaction with a QIB without itself having to be a QIB.

A “QIB” also includes any entity, all of the equity owners of which are QIBs, acting for its own account or the accounts of other QIBs.

Generally, any instrument that, but for a specific exemption, would have to be registered with the SEC under the Securities Act may be counted toward the amount of securities required to be owned and invested on a discretionary basis, including, for example, U.S.-issued or -guaranteed securities, asset-backed securities and securities issued or guaranteed by international development banks. However, not included are: bank deposit notes and certificates of deposit, loan participations, repurchase agreements, securities owned but subject to a repurchase agreement, and currency, interest rate and commodity swaps.

To establish a reasonable belief that a prospective purchaser is a QIB, a seller (and any person acting on its behalf) may rely on: (i) the prospective purchaser’s most recent publicly available financial statements; (ii) the most recent publicly available information appearing in documents filed by the prospective purchaser with the SEC or another U.S. federal, state or local governmental agency or self-regulatory organization (e.g., a securities exchange), or with a foreign governmental agency or self-regulatory organization; (iii) the most recent publicly available information appearing in a recognized securities manual; or (iv) a certification by the purchaser’s chief financial officer (or other executive officer) that specifies the amount of securities owned and invested on a discretionary basis by the purchaser as of a specific date on or since the close of the purchaser’s most recent fiscal year. For categories (i) through (iii) above, the information must be as of a date not more than 16 months before the date of sale (18 months for a foreign purchaser).

(b) Notice of Possible Reliance. The seller (and any person acting on its behalf) must take reasonable steps to ensure that the purchaser is aware that the seller may be relying on Rule 144A.

(c) Non-Fungible Securities. When initially issued, the securities sold cannot be fungible with exchange-listed securities or securities quoted in a U.S. automated inter-dealer quotation system. Convertible securities with less than a 10% conversion premium are considered fungible with the underlying security. This is more of a concern for common equity than debt or preferred stock because relatively few debt or preferred stock issues are listed or quoted.

(d) Information. If the issuer is neither subject to the reporting requirements of the Exchange Act (U.S. and foreign issuers) nor exempt from those requirements under Rule 12g3-2(b) under the Exchange Act (foreign issuers), it must undertake to make “reasonably current” information about itself available to each holder and to any prospective purchaser from a holder. The required information consists of: (i) a very brief statement of the nature of the issuer’s business and its products and services; and (ii) the issuer’s most recent balance sheet and profit and loss and retained earnings statements, and similar financial statements for the part of the two preceding fiscal years as the issuer has been in operation. The financial statements should be audited to the extent reasonably available. The requirement that the information be

“reasonably current” will be presumed to be met if: (i) the balance sheet is as of a date less than 16 months before the date of resale and the statements of profit and loss and retained earnings are for the 12 months preceding the date of the balance sheet (however, if the balance sheet is not as of a date less than six months before the date of resale, it must be accompanied by additional statements of profit and loss and retained earnings for the period from the date of the balance sheet to a date within six months of the resale); and (ii) the statement of the nature of the issuer’s business and its products and services offered is as of a date within 12 months before the date of resale; or (iii) for foreign private issuers, the required information meets the timing requirements of the issuer’s home country or principal trading markets.

(e) No Investment Companies. The issuer of the securities cannot be an open-end investment company, a unit investment trust, or a face-amount certificate company that is or is required to be registered under Section 8 of the Investment Company Act.

(f) No General Solicitation. While not expressly stated, it appears that resales under Rule 144A may not involve general solicitation.

4. Issues Related to Rule 144A

(a) The PORTAL Market. The PORTAL Market was NASDAQ’s centralized market for primary offerings (under Section 4(2) or Regulation D) and secondary trading of unregistered securities under Rule 144A, which also provided clearance and settlement facilities through the Depository Trust Company (“DTC”). Participation in the PORTAL Market was limited to NASDAQ Stock Market LLC members and to QIBs who registered with NASDAQ as PORTAL qualified investors.

In September 2008, NASDAQ ceased the operation of the PORTAL Market. In doing so, NASDAQ explained that it was taking a minority stake in a consortium that would control and operate a new electronic platform for handling transactions in Rule 144A-eligible securities. In addition to NASDAQ ceasing operation of the PORTAL Market, the SEC also approved the deletion of the DTC requirement that a Rule 144A security, other than investment grade securities, be included in an “SRO Rule 144A System” in order to be eligible for DTC’s deposit, book-entry delivery and other depository services.

On October 26, 2009, NASDAQ terminated the PORTAL security designation process and removed rules related to the PORTAL Market from its rulebook. Although, as of October 26, 2009, NASDAQ no longer accepted new applications for debt or equity securities seeking PORTAL designation, the termination of this function was not “intended to impact securities previously designated as PORTAL securities or alter any existing regulatory obligation applicable to such securities, including, but not limited to, any trade reporting obligation imposed by any self-regulatory organization.”

Although securities previously designated as PORTAL securities remained subject to the reporting requirements in the PORTAL rules, the cessation of the designation of securities as PORTAL securities created a gap in FINRA’s transaction reporting requirements for restricted equity securities that are traded under Rule 144A. To address this gap, effective June 28, 2010, the PORTAL reporting rules are eliminated and the OTC Reporting

Facility (“ORF”) rules include reporting requirements for all equity securities that are defined as “restricted securities” under Rule 144(a)(3) and are traded under Rule 144A, irrespective of whether they are designated as PORTAL securities. Beginning on that date, transactions in all restricted equity securities effected under Rule 144A must be reported to the ORF no later than 8 p.m. Eastern Time. Transactions in restricted equity securities effected under Rule 144A and executed between 8 p.m. and midnight must be reported the following business day (T+1) by 8 p.m. See also FINRA Rule 6630 (Applicability of FINRA Rules to Securities Previously Designated as PORTAL Securities).

(b) Regulation M. Regulation M (adopted under the Securities Act, the Exchange Act and the Investment Company Act) contains anti-manipulation rules that regulate certain trading practices during a securities distribution in the United States. Generally, Regulation M is designed to prevent the price of a security being distributed from being raised artificially by someone with an interest in the distribution.

Rule 144A offerings to QIBs are excepted from Regulation M because such offerings are considered not to constitute “distributions” of a security.

F. Regulation S

1. Offshore Resales. Rule 904 of Regulation S is a safe harbor from the registration requirement of Section 5 of the Securities Act for resales of securities made in “offshore transactions” (i.e., not offered to any person in the United States and executed in an offshore market) with no “directed selling efforts” in the United States by the seller, an affiliate or any person acting on their behalf, plus, for dealer sales during the “distribution compliance period” specified in Category 2 or 3 of Rule 903 of Regulation S (discussed in Chapter 8), with no knowledge by the seller or any person acting on its behalf that the offeree or buyer is a “U.S. person.” Rule 904 is available for offers and sales of securities by any person other than the issuer, a distributor, any of their respective affiliates (except any officer or director who is an affiliate solely by virtue of holding such position) or any person acting on behalf of any of the above.

2. Resale Limitations. Under Rule 905 of Regulation S, equity securities of U.S. issuers acquired from the issuer, a distributor or any of their respective affiliates in an offshore transaction under Rule 901 or Rule 903 of Regulation S are “restricted securities” within the meaning of Rule 144 (i.e., as a practical matter, they must be resold under Rule 144 when resold in the United States). And, offshore resales of such securities under Rule 904 (or Rule 901) will not “wash-off” their “restricted” status.

G. Rule 144A’s Interaction with Regulation S

1. Resales of 144A Securities Outside the United States: Generally, securities in the United States acquired under Rule 144A may be immediately resold outside the United States under Rule 904 (the “Resale Safe Harbor” of Regulation S); i.e.,

- (a) the offer and sale must be made in an “offshore transaction,” and

(b) no “directed selling efforts” may be made in the United States by the seller, an affiliate or any person acting on their behalf.

2. Resales of Regulation S Securities into the United States under Rule 144A: The Section 4(3) dealer 40-day prohibition applies to resales into the United States of securities sold outside the United States, but Rule 144A resales can be made throughout the Section 4(3) dealer prohibition period. Consequently, securities offered and sold outside the United States without registration under Regulation S may be resold immediately in the United States by dealers to QIBs under Rule 144A. There is no need to comply with any Regulation S “distribution compliance period” or the Section 4(3) 40-day period. All such securities will be “restricted securities” in the hands of the QIB purchaser.

3. Resales of Regulation S Securities into the United States under the Section 4(1½) Exemption: By comparison, securities sold outside the United States cannot be resold in the United States by a dealer under the Section 4(1½) exemption during the 40-day Section 4(3) dealer prohibition period.

H. Resales After Business Combinations

1. Rule 145(a) under the Securities Act specifies that an offer and sale of securities occurs in any transaction in which a plan or agreement of merger or consolidation (accompanied by an exchange of securities), asset transfer (accompanied by a distribution of securities) or reclassification (involving the substitution of one security for another) is submitted to a statutory vote of the security holders of a corporation. (See Chapter 4.)

2. Formerly, under Rule 145(c), persons who were parties to such a transaction, other than the issuer, or affiliates of such parties, were deemed to be “underwriters.” (This is called the “presumptive underwriter provision.”) Rule 145(d) permits the resale of securities received in such transactions by persons deemed underwriters if certain conditions are met.

3. In 2008, the SEC eliminated the presumptive underwriter provision of Rule 145(c) except for Rule 145(a) transactions involving a shell company (discussed in 4. below). Rule 145(c) had been used to limit resales by affiliates of a company that was a party to a Rule 145(a) business combination. These affiliates were presumptive underwriters, and as such, could not resell securities acquired in the Rule 145(a) transaction without meeting the volume, manner of sale and other limitations of Rule 145(d). Rule 145(c), as amended, allows affiliates of a company that is a party to a Rule 145(a) transaction (who do not immediately become affiliates of the acquiror) to immediately resell the securities received in the transaction without regard to the volume, manner of sale and other restrictions of Rule 145(d). These affiliates are also able to hedge their positions before the closing of the transaction as a result of this amendment.

4. Because of the SEC’s experience with abusive sales of securities involving shell companies, Rule 145(c) provides that any party, other than the issuer, to a Rule 145(a) transaction involving a shell company (other than a business combination related shell company), including any affiliate of such party, who publicly offers or sells securities of the issuer acquired in connection with the transaction, will continue to be deemed an underwriter. However, under Rule 145(d), if the issuer meets the conditions of Rule 144(i)(2) (i.e., that Form

10 information is filed indicating that the company is no longer a shell company), the presumptive underwriters may resell their securities if: (a) the current public information, volume limitation and manner of sale requirements of Rule 144 are met and at least 90 days have elapsed since the securities were acquired in the Rule 145(a) transaction; or (b) the seller is not an affiliate of the issuer at the time of sale and has not been an affiliate during the three months before the sale, at least six months have elapsed since the securities were acquired in the Rule 145(a) transaction, and the Rule 144 current public information condition is met; or (c) the seller is not an affiliate of the issuer at the time of sale and has not been an affiliate during the three months before the sale, and at least one year has elapsed since the securities were acquired in the Rule 145(a) transaction.

5. Like Rule 144, Rule 145(d) is not available for any transaction or series of transactions that, although in technical compliance with the Rule, is part of a plan or scheme to evade the registration requirements of the Securities Act.

I. Resales After Bankruptcy

11 U.S.C. § 1145 contains special rules for determining “underwriter” status for resales of securities received under plans confirmed under Chapter 11 of the U.S. Bankruptcy Code.

11 U.S.C. § 1145(b)(1) provides that, with limited exceptions, an entity is an “underwriter” under Section 2(a)(11) of the Securities Act if the entity: (a) purchases claims against or interests in the debtor corporation “with a view to distribution of any security received or to be received in exchange for such a claim or interest”; (b) offers to sell securities offered or sold under the Chapter 11 plan for the holders of such securities; (c) offers to buy securities offered or sold under the Chapter 11 plan from the holders of such securities, if such offer to buy is: (i) “with a view to distribution of such securities,” and (ii) under an agreement made in connection with the plan, with the consummation of the plan, or with the offer or sale of securities under the plan; or (d) is an issuer, as used in Section 2(a)(11), with respect to such securities. (As used in Section 2(a)(11) the term “issuer” includes, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.)

11 U.S.C. § 1145(b)(3) provides that an entity other than an entity of the kind specified above is not an underwriter under Section 2(a)(11) with respect to any securities offered or sold to that entity in the manner specified in 11 U.S.C. § 1145(a)(1). 11 U.S.C. § 1145(a)(1) provides that, except for an entity that is an underwriter under 11 U.S.C. § 1145(b), Section 5 of the Securities Act and any State or local law requiring registration for offer or sale of a security do not apply to the offer or sale under a Chapter 11 plan of a security of the debtor, of an affiliate participating in a joint plan with the debtor, or of a successor to the debtor under the plan: (a) in exchange for a claim against, an interest in, or a claim for an administrative expense in the case concerning, the debtor or such affiliate; or (b) principally in such exchange and partly for cash or property.

J. Registration Under the Securities Act

If an exemption under the Securities Act is not available for the resale of securities by an

affiliate of an issuer or by a holder of restricted securities, the resale must be registered under the Securities Act.

1. Form S-3 or F-3

Form S-3 or F-3 is a short form of registration statement. If the applicable requirements are met, it can be used by an issuer in an initial offering, by an affiliate to resell securities of an issuer, or by any person to resell restricted securities.

2. Form S-1 or F-1

Form S-1 or F-1 is the general form prescribed for use in all offerings where no other form is authorized. If no other form is available, resales of securities held by affiliates or resales of restricted securities held by any person have to be registered on Form S-1 or F-1. As a result of the lengthy disclosure required by Form S-1 or F-1 and the review required by the SEC, registration on Form S-1 or F-1 involves significantly more time and expense than registration on Form S-3 or F-3.

3. Form S-4 or F-4

Form S-4 or F-4 is the form used when a holder of restricted securities exchanges its restricted securities for similar securities issued in a registered exchange offer. The registered securities may then be freely resold.

4. MJDS Form F-10

Form F-10 is the general MJDS form prescribed for registration of any security of a Canadian issuer where no other form is authorized.

CHAPTER 8.

REGULATION S

A. Introduction

Regulation S is a series of rules (Rules 901-905 under the Securities Act) that clarify when securities offered and sold outside the United States need not be registered with the SEC under Section 5 of the Securities Act.

Read literally, the registration requirement of Section 5 of the Securities Act applies to any offer or sale of a security involving the use of the U.S. mails or any means of “interstate commerce.” Interstate commerce is defined to mean commerce among the several states and commerce between any foreign country and any state. Consequently, the Securities Act does not apply to sales totally outside the United States. But, it does apply to sales into the United States by non-U.S. companies and to sales outward from the United States into other countries by U.S. and non-U.S. companies.

Regulation S reflects the decision of the SEC not to exercise administrative jurisdiction to require registration when securities are offered and sold outside the United States despite incidental U.S. conduct or even U.S. roots. The SEC believed that persons inside the United States might need anti-fraud protection but not the protections afforded by registration.

For sales of securities outside the United States, the SEC was concerned about “flowback” into the United States. Generally, securities tend to flow back to their home country market, particularly in times of stress. The sale of securities in anticipation of flowback, i.e., immediate flowback, into the United States, whether because the sole or predominant market is in the United States, is viewed by the SEC as evidence of impermissible evasion of the registration requirement. Therefore, where there is a realistic expectation of flowback after initial sales abroad, the SEC applies the definition of “underwrites” which would result in a statutory violation in resale. This occurs for sales outside the United States by U.S. companies and non-U.S. companies whose principal equity market is in the United States.

In light of these concerns, Regulation S provides two safe harbors for permissible offers and sales of securities deemed to be outside the United States--Rule 903, the “Issuer and Affiliate Safe Harbor,” and Rule 904, the “Resale Safe Harbor.”

B. General Statement

The General Statement in Rule 901 of Regulation S states the territoriality principle, i.e., that offers and sales that occur within the United States are subject to Section 5 of the Securities Act while those that occur outside the United States are not subject to Section 5. The determination whether a transaction is outside the United States is based on the facts and circumstances of each case. If it can be demonstrated that both the offer and sale of the securities occurred outside the United States, Section 5 will not apply regardless of whether the conditions of a safe harbor were met. Although all transactions should be structured to meet the conditions of one of the safe harbors of Regulation S, a person could rely on the General Statement if a safe harbor condition was inadvertently not met.

C. General Conditions of Both Safe Harbors

The prerequisites for both safe harbors are that all offers and sales must be: (a) in Offshore Transactions, and (b) with no Directed Selling Efforts in the United States.

D. Definitions

1. “Offshore Transactions” are transactions where:

(a) the offer is not made to a person in the United States; and

(b) either: (i) when the buy order is originated, the buyer is outside the United States, or the seller and any person acting on its behalf reasonably believe that the buyer is outside the United States; or (ii) for: (A) Rule 903 (the Issuer and Affiliate Safe Harbor), the transaction is executed in, on or through a physical trading floor of an established foreign securities exchange that is located outside the United States; or (B) Rule 904 (the Resale Safe Harbor), the transaction is executed in, on or through the facilities of one of a number of offshore securities markets designated by the SEC (which include various markets around the world, such as the London Stock Exchange, the Tokyo Stock Exchange, the Australian Stock Exchange Limited, the Toronto Stock Exchange, and many others), and neither the seller nor any person acting on its behalf (e.g., the seller’s broker) knows that the transaction has been prearranged with a buyer in the United States.

2. “Directed Selling Efforts” include, subject to very limited exceptions, any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the market in the United States for any of the securities being offered outside the United States in reliance on Regulation S.

3. “Substantial U.S. Market Interest” is present for a class of an issuer's equity securities if either:

(a) the securities exchanges and inter-dealer quotation systems in the United States in the aggregate constituted the single largest market for the class of securities in the shorter of the issuer's prior fiscal year or the period since the issuer's incorporation; or

(b) 20% or more of all trading in the class of securities took place in, on or through the facilities of securities exchanges and inter-dealer quotation systems in the United States and less than 55% of such trading took place in, on or through the facilities of securities markets of a single foreign country in the shorter of the issuer's prior fiscal year or the period since the issuer's incorporation.

Another test applies to debt securities.

E. Rule 903: The Issuer and Affiliate Safe Harbor

1. Introduction

Rule 903 is the safe harbor for offshore offers and sales by: (a) the issuer, (b)

distributors, (c) their respective affiliates, and (d) persons acting on behalf of (i.e., agents of) any of the above. It applies to primary sales and is divided into three categories.

2. General Conditions

For all three categories, all offers and sales must be made: (a) in Offshore Transactions; and (b) with no Directed Selling Efforts in the United States by the issuer, any “distributor” (i.e., any underwriter, selling group member or other participant in the distribution under contract), any of their respective affiliates or any agent of any of the above.

3. The 3 Categories

(a) Category 1: There are no conditions other than the two General Conditions above for:

- (i) offerings by foreign issuers with no SUSMI (i.e., Substantial U.S. Market Interest)--if equity is sold, in the class of securities to be sold; if debt is sold, in the issuer’s debt securities; if warrants are sold, in the underlying securities to be purchased on exercise; if convertibles are sold, in either the convertibles or the underlying securities. Most foreign issuers find they do not have SUSMI, even if their securities are traded in the United States;
- (ii) overseas directed offerings, which means: (A) an offering of securities of a foreign issuer (even one with SUSMI) that is directed to residents of a single foreign country under the laws, practices and documentation of that country; or (B) an offering of non-convertible debt securities (or non-participatory preferred stock or asset-backed securities) of a U.S. issuer that is directed to residents of a single foreign country under the laws, practices and documentation of that country, provided that the principal and interest of the securities (or par value, as applicable) are denominated in a currency other than U.S. dollars and the securities are neither convertible into U.S. dollar-denominated securities nor linked to U.S. dollars (other than through related currency or interest rate swap transactions that are commercial in nature) in a manner that in effect converts the securities to U.S. dollar-denominated securities;
- (iii) offerings of securities backed by the full faith and credit of a foreign government; and
- (iv) offerings of securities to employees of the issuer or its affiliates under an employee benefit plan established and administered under the laws, practices and documentation of a foreign country. However, to qualify under (iv), the following conditions must be met: (A) the securities must be issued in compensation for bona fide services rendered to the issuer or its affiliates in connection

with their businesses and not in connection with the offer or sale of securities in a capital-raising transaction; (B) any interests in the plan cannot be transferred except by will or by the laws of descent or distribution; (C) the issuer must take reasonable steps to prevent the offer and sale of interests in the plan or securities under the plan to U.S. residents (except employees on temporary assignment in the United States); and (D) documentation used in connection with any offer under the plan must contain a statement that the securities have not been registered under the Securities Act and may not be offered or sold in the United States except after registration or under an available exemption from registration.

There is no “distribution compliance period” (discussed below) for securities in Category 1. But, Section 4(3) may prohibit broker-dealers from trading the securities as principal for 40 days, except for Rule 144A transactions.

(b) Category 2: Category 2 offerings of securities can be made outside the United States provided they are eligible and comply with certain restrictions.

(i) Eligible Offerings

- (A) equity offerings by reporting foreign issuers;
- (B) debt offerings by reporting issuers (U.S. or foreign); and
- (C) debt offerings by non-reporting foreign issuers.

Thus, Category 2 of the Issuer and Affiliate Safe Harbor covers: (1) equity offerings by reporting foreign issuers where the offering does not qualify for Category 1 (e.g., where there is SUSMI in the class of securities to be sold and Category 1 does not otherwise apply); (2) debt offerings by reporting and non-reporting foreign issuers where the offering does not qualify for Category 1 (e.g., where there is SUSMI in the foreign issuer's debt securities and Category 1 does not otherwise apply); and (3) debt offerings by reporting U.S. issuers where the offering does not qualify for Category 1 (i.e., where the offering is not an “overseas directed offering”). Additionally, Category 2 is available where the offering is of a kind covered by (A), (B), or (C) above, but the issuer is not sure whether the offering qualifies for Category 1.

(ii) Selling Restrictions

- (A) there is a 40-day “distribution compliance period” during which no offers or sales may be made to or for a U.S. person (other than a distributor);
- (B) during the distribution compliance period (and indefinitely, for unsold allotments), each distributor must send a confirmation or other notice stating that the purchaser (if a distributor, dealer or person receiving remuneration with

respect to the securities) is subject to the same restrictions on offers and sales that apply to the distributors; and

- (C) offering restrictions are implemented to assure that any securities resold are either registered under the Securities Act or exempt from registration. (The offering restrictions are discussed below.)

(c) Category 3: Category 3 is the residual category (i.e., it covers those securities offerings not covered by Categories 1 and 2). In effect, this category covers: (1) equity offerings by reporting and non-reporting U.S. issuers, (2) equity offerings by non-reporting foreign issuers where there is SUSMI in the class of securities to be sold and the offering does not otherwise qualify for Category 1, and (3) debt offerings by non-reporting U.S. issuers that do not qualify for Category 1. To protect against an unregistered U.S. distribution when there is a significant likelihood of flowback, this category requires procedures in addition to the two General Conditions and other restrictions of Category 2.

- (i) Selling Restrictions. Category 3 offerings must meet certain selling restrictions as in Category 2:

- (A) there is a 40-day “distribution compliance period” for debt and a one-year “distribution compliance period” for equity (the “distribution compliance period” for equity is six months if the issuer is a reporting issuer) during which no offers or sales may be made to or for a U.S. person (other than a distributor);
- (B) during the distribution compliance period (and indefinitely, for unsold allotments), each distributor must send a confirmation or other notice stating that the purchaser (if a distributor, dealer or person receiving remuneration with respect to the securities) is subject to the same restrictions on offers and sales that apply to the distributors; and
- (C) offering restrictions are implemented. To comply with the conditions of Categories 2 and 3 of the Issuer and Affiliate Safe Harbor, offering restrictions must be implemented by the issuer, distributors, their respective affiliates and persons acting on behalf of any of them. The failure to implement the offering restrictions precludes the availability of the safe harbor for everyone. Each distributor (i.e., each underwriter, selling group member, and other participant in the distribution under contract) must agree in writing: (1) to make all of its offers and sales during the applicable distribution compliance period in accordance with Rule 903 or 904 of Regulation S, after registration under the Securities Act or under an available

exemption from registration; and (2) for offers and sales of equity securities of U.S. issuers, not to engage in hedging transactions for those securities during the applicable distribution compliance period, except in compliance with the Securities Act. Furthermore, all offering materials and documents (other than press releases) used in connection with offers and sales of the securities during the applicable distribution compliance period (including prospectuses, offering circulars and advertisements) must include statements: (1) that the securities have not been registered under the Securities Act and may not be offered or sold in the United States or to U.S. persons (other than distributors) unless the securities are registered under the Securities Act or an exemption from registration is available; and (2) for offers and sales of equity securities of U.S. issuers, that hedging transactions involving those securities may not be made, except in compliance with the Securities Act. These statements must appear: (1) on the cover or inside cover page of any prospectus or offering circular used in the offering; (2) in the underwriting section of any prospectus or offering circular used in the offering; and (3) in any advertisement made or issued by the issuer, any distributor, any of their respective affiliates or any person acting on behalf of any of them. These statements may appear in summary form on prospectus cover pages and in advertisements.

(ii) Transactional Restrictions

Additionally, “transactional restrictions” must be adopted:

- (A) Debt Securities. Debt securities must be represented on issuance by a temporary global security that is not exchangeable for definitive securities until the 40-day distribution compliance period expires and, for non-distributors, until certification of beneficial ownership of the securities by a permitted buyer (i.e., by a non-U.S. person or by a U.S. person who purchased the securities in a transaction that did not require registration under the Securities Act).
- (B) Equity Securities. Equity securities may be offered and sold before the one-year (or six month) distribution compliance period expires, in accordance with the following conditions:

(1) the purchaser (other than a distributor) must certify that it is a permitted buyer (i.e., that it is not a U.S. person and is not acquiring the securities for the account or benefit of any U.S. person, or that it is a U.S. person who purchased its securities in an exempt transaction);

(2) the purchaser must agree: (I) to resell the securities only in accordance with Regulation S, after registration or under an exemption; and (II) not to engage in hedging transactions for those securities, except in compliance with the Securities Act (e.g., under Rule 144);

(3) securities of a U.S. issuer must contain a legend stating: (I) that transfer is prohibited except in accordance with Regulation S, after registration or under an exemption; and (II) that hedging transactions involving those securities may not be made, except in compliance with the Securities Act; and

(4) the issuer must be required (either by contract, or by a provision in its bylaws, articles, charter or comparable document) to refuse to register any transfer of the securities that is not made in accordance with Regulation S, after registration or under an exemption. However, if the securities are in bearer form, or if foreign law prevents the issuer from refusing to register securities transfers, other reasonable procedures (such as the legend described in (3) above) must be implemented to prevent any transfer of the securities not made in accordance with Regulation S.

Note that warrants may not be exercised in the United States or by a U.S. person unless the underlying securities are registered under the Securities Act or an exemption from registration is available. Further, issuers relying on Regulation S to cover the exercise of the warrants may have to refrain from Direct Selling Efforts for the life of the warrants.

F. Rule 904: The Resale Safe Harbor

Rule 904 provides a safe harbor for resales outside the United States. Rule 904 is available for offers and sales of securities by persons other than the issuer, distributors, certain of their respective affiliates and persons acting on behalf of any of them. Under Rule 904, resales by (a) any person other than the issuer, a distributor, any of their respective affiliates and any person acting on behalf of any of them, and (b) any officer or director of the issuer or a distributor who is an affiliate solely by virtue of holding such position, are deemed to occur outside the United States if the two General Conditions are met (i.e., if the offers and sales are made in “Offshore Transactions” (see D.1. above) and no “Directed Selling Efforts” (see D.2. above) are made in the United States by the seller, an affiliate or any person acting on their behalf).

Officers and directors who are affiliates solely by virtue of their positions (i.e., not because of their security holdings) may rely on Rule 904, and other affiliates must comply with the requirements of Rule 903 (i.e., the Issuer and Affiliate Safe Harbor). However, officers and directors who qualify for Rule 904 must pay only the customary broker's commission that would be received by a person executing the transaction as agent. In other words, persons who are affiliates of the issuer or a distributor solely by virtue of being executive officers and directors (and not by virtue of owning a substantial amount of securities) may resell securities under Rule 904 provided no commission, selling concession or other compensation is paid for the sale other than a normal brokerage commission.

Resales under Rule 904 during the applicable distribution compliance period by a dealer or other person receiving a selling concession, fee or other remuneration for the securities sold (such as a sub-underwriter) are permitted if, in addition to the two General Conditions, the following conditions are met: (a) neither the seller nor any person acting on its behalf knows that the offeree or buyer of the securities is a U.S. person; and (b) where the seller or any person acting on its behalf knows that the purchaser is a dealer or other person receiving a selling concession, fee or other remuneration for the securities sold, the seller (or a person acting on the seller's behalf) sends to the purchaser a confirmation or other notice stating that the securities may be offered and sold during the distribution compliance period only in accordance with Regulation S, after registration under the Securities Act or under an exemption from registration.

The Resale Safe Harbor is available for the resale of any securities outside the United States, whether or not acquired offshore in a Regulation S transaction. For example, securities acquired in a Rule 144A or other private placement transaction may be immediately resold under the Rule 904 Resale Safe Harbor.

G. Rule 905: Status

Rule 905 states: (a) that equity securities of U.S. issuers that were previously acquired in a Rule 901 (General Statement) or Rule 903 (Issuer and Affiliate Safe Harbor) transaction are “restricted securities” under Rule 144 (i.e., generally required to be resold under Rule 144 when resold in the U.S. public markets); and (b) that offshore resales of such securities under Rule 901 (the General Statement) or Rule 904 (the Resale Safe Harbor) will not wash-off their status as “restricted securities.” Consequently, equity securities of U.S. issuers resold under Regulation S are restricted. But, securities of foreign private issuers resold under Regulation S are not restricted.

CHAPTER 9.

EXCHANGE ACT REGISTRATION AND REPORTING

A. Introduction

Generally, every public company must file periodic reports with the SEC under the Exchange Act. These reports basically update the information in the company's registration statement by periodically updating information about the company and providing the company's shareholders and the general public with material, current information, which facilitates trading of the company's securities.

B. Registration Under the Exchange Act

1. Section 12 of the Exchange Act: The Registration Requirement

Registration under Section 12 of the Exchange Act of a class of securities of an issuer is required where:

(a) Exchange Listed Securities. The securities are to be listed on a U.S. stock exchange or quoted on the OTC Bulletin Board; or

(b) Widely Held Securities. The class of equity securities is "widely held" (i.e., is held by at least 500 shareholders of record, at least 300 of whom are U.S. residents) and the issuer has total assets exceeding \$10 million. In determining the number of U.S. holders, securities held of record by brokers, dealers, banks or other nominees for the account of holders resident in the United States are counted as held by the number of separate accounts for which the securities are held.

2. Section 15(d) of the Exchange Act: Issuers That Made a U.S. Registered Offering

Any issuer that registers its securities under the Securities Act must file periodic Exchange Act reports (as if its securities were registered under the Exchange Act). However, this reporting obligation is automatically suspended for any fiscal year following the year of registration if, at the beginning of that year, the class of securities is held of record by less than 300 persons in the United States.

3. Voluntary Registration

Oftentimes an issuer of debt securities is required under the indenture to voluntarily register a class of securities under the Exchange Act. Additionally, a foreign private issuer may voluntarily register a class of its securities under the Exchange Act. In that case, the reasons for doing so may include obtaining the protection of certain Exchange Act tender offer provisions or an underwriter's requirement to register before undertaking an offering.

4. Rule 12g3-2(b) under the Exchange Act: the Information Supplying Exemption from Exchange Act Registration

Rule 12g3-2(a) under the Exchange Act exempts foreign private issuers from

registration under Section 12(g) of the Exchange Act (see B.1.(b) above) without conditions if the issuer does not have 300 holders of record resident in the United States at fiscal year end. (However, when securities are held of record for U.S. residents in street name by broker-dealers or banks, the issuer must inquire as to the ownership of those securities and the security holders are determined based on the number of separate accounts for which the securities are held. Additionally, if the issuer is aware of the existence of an ADR facility for its bearer equity securities, the issuer must contact the depositary for the ADR facility, request the number of U.S. security holders on the depositary's records, and include this figure in its total number of U.S. security holders. Further, for this exemption, persons in the United States who hold the security only through a Canadian Retirement Account will not be counted as holders resident in the United States.)

Rule 12g3-2(b) permits foreign private issuers that exceed the asset and shareholder thresholds for registration under Section 12(g) of the Exchange Act to exceed the 300 U.S. holders limit if the conditions of the Rule (discussed below) are met.

(An issuer deregistering under Rule 12h-6 under the Exchange Act can rely on Rule 12g3-2(b).)

(a) Eligibility for the Rule 12g3-2(b) Exemption. The exemption is granted automatically if a foreign private issuer:

- (i) Foreign listing. Maintains a listing of the securities on an exchange outside the United States that constitutes the primary trading market for those securities (specifically, maintains a listing of the subject class of securities on one or more exchanges in a foreign jurisdiction that, either singly or together with the trading of the same class of the issuer's securities in one other foreign jurisdiction, constitutes the primary trading market for those securities);⁹²
- (ii) Electronic availability of required disclosure. Publishes in English, either on its Internet web site or through an electronic information delivery system that is generally available to the public in its primary trading market (e.g., SEDAR), one year's worth of its non-U.S. disclosure documents (i.e., information that, from the first day of its mostly recently completed fiscal year, it: (A) has made public or been required to make public under the laws of the country of its incorporation, organization or domicile; (B) has filed or been required to file with the principal stock exchange in its primary

⁹² For Rule 12g3-2(b), "primary trading market" means that at least 55 percent of the worldwide trading in the issuer's subject class of securities took place in, on or through the facilities of a securities market or markets in a single foreign jurisdiction or in no more than two foreign jurisdictions during the issuer's most recently completed fiscal year. Additionally, if the foreign private issuer aggregates the trading of its subject class of securities in markets in two foreign jurisdictions, the trading in the securities in the markets of at least one of the two foreign jurisdictions must be larger than the trading in the U.S. markets in those securities.

trading market on which its securities are traded and which has been made public by that exchange; and (C) has distributed or been required to distribute to its security holders);⁹³ and

- (iii) Has no Exchange Act reporting obligation.

SEDAR makes this rule work very smoothly for Canadian issuers.

This is a self-executing exemption; there is no evidence of the exemption granted by the SEC.

- (b) Maintaining the Exemption. To maintain the exemption, an issuer must:
 - (i) Maintain its non-U.S. listing in its primary trading market;
 - (ii) Electronically publish its non-U.S. disclosure documents; and
 - (iii) Not incur any Exchange Act reporting obligation.

C. Registration and Reporting Under the Exchange Act

1. General

Registration under Section 12 of the Exchange Act results in an issuer being subject to the reporting obligations of Section 13 of the Exchange Act. Under Section 15(d), registering securities under the Securities Act also results in reporting under Section 13. However, foreign private issuers are not subject to Section 14 proxy regulation or Section 16 insider reporting and short-swing profit recapture under the Exchange Act.

2. Registration and Reporting for U.S. Companies and Non-U.S. Companies That Are Not Foreign Private Issuers

(a) U.S. issuers and non-U.S. issuers that do not qualify as “foreign private issuers” must register and report in the same manner as follows:

- (i) Registration Statement: Form 10. The basic registration statement for securities under the Exchange Act is Form 10. It must be filed by the company within 120 days after the first fiscal year-end at which the criteria for registration are met.

⁹³ The information required to be published electronically under (ii) in the text is information that is material to an investment decision concerning the subject securities, such as: results of operations or financial condition; changes in business; acquisitions or dispositions of assets; the issuance, redemption or acquisition of securities; changes in management or control; the granting of options or the payment of other remuneration to directors or officers; and transactions with directors, officers or principal security holders.

- (ii) Annual Report: Form 10-K. An annual report on Form 10-K must be filed by the issuer as follows:
 - (A) if the issuer is a “large accelerated filer” (defined below), within 60 days after the end of the fiscal year;
 - (B) if the issuer is an “accelerated filer” (defined below), within 75 days after the end of the fiscal year; and
 - (C) for all other registrants, within 90 days after the end of the fiscal year.

Form 10-K must include audited financial statements. The financial statements consist of balance sheets as of the end of the two most recent fiscal years and statements of income and cash flow for each of the three fiscal years preceding the date of the most recent audited balance sheet being filed. The financial statements must be prepared under U.S. GAAP.

The Form 10-K is intended to provide current information about the company that is generally comparable to the information included in the registration statement when the issuer went public, including audited financial information for the year and an MD&A (management’s discussion and analysis of financial condition and results of operations, discussed later), but excluding certain disclosure such as the “Underwriting” and “Description of Capital Stock” sections that appeared in the registration statement. Additionally, the Form 10-K must contain an updated narrative description of the issuer’s business, properties, legal proceedings, management, principal shareholders, executive compensation, transactions between the issuer and its management or principal shareholders and other material events. Additional information required to be included in the Form 10-K but that was not a part of the registration statement includes a summary of the high and low prices of the common shares during various periods of time. Some information may be omitted from the Form 10-K and incorporated by reference to the issuer’s proxy statement, provided a definitive proxy statement is filed with the SEC within 120 days after the end of the fiscal year covered by the Form 10-K.

The Form 10-K must be signed by the issuer’s chief executive officer, principal financial officer, comptroller or principal accounting officer, and by at least a majority of the directors. Although the members of the audit committee of the board of directors will be specifically charged with overseeing the audit process from the board’s perspective, all of the directors have a responsibility to review the Form 10-K to make certain that the disclosure is accurate, complete and not misleading. The Form 10-K should be prepared sufficiently in advance of the filing deadline so that copies may be circulated to all directors for their review and approval before filing.

- (iii) Quarterly Report: Form 10-Q. A quarterly report on Form 10-Q must be filed by the issuer after the end of each of the first three fiscal quarters of each fiscal year as follows:
 - (A) if the issuer is a “large accelerated filer” or an “accelerated filer” (defined below), within 40 days after the end of the fiscal quarter; and
 - (B) for all other registrants, within 45 days after the end of the fiscal quarter.

Form 10-Q includes an unaudited balance sheet as of the end of the quarter and income statements for the quarter and year-to-date and for comparable periods in the prior fiscal year, and MD&A of these statements. The interim financial statements must be reviewed by the issuer’s independent auditors. The MD&A should explain material changes in revenue and expense items in the relevant quarter and, if applicable, the current year to date, as compared to the same quarter in the prior fiscal year and, if applicable, the same period in the prior fiscal year. The Form 10-Q must also discuss other material events that occurred during the quarter (such as newly instituted, reportable legal proceedings, changes in securities (including private sales of equity securities of the company during the period covered by the report) and reports of shareholder actions and other events).

Following effectiveness of an issuer’s first registration statement under the Securities Act, the issuer must report how it used the proceeds of the offering in each periodic report (Form 10-Q or 10-K) filed under the Exchange Act until the later of disclosure of the application of all the proceeds or disclosure of the termination of the offering.

- (iv) Large Accelerated Filers. A public company will be a “large accelerated filer” if as of the last business day of its fiscal year:
 - (A) it has a public float of common equity of \$700 million or more, computed as of the last business day of its most recently completed second fiscal quarter (i.e., June 30 for issuers with December 31 fiscal year ends);
 - (B) it has been subject to the reporting requirements of the Exchange Act for at least 12 calendar months;
 - (C) it has previously filed at least one annual report under the Exchange Act; and
 - (D) it is not eligible to use the requirements for smaller reporting companies in Regulation S-K for its annual and quarterly reports.

- (v) Accelerated Filers. A public company will be an “accelerated filer” if as of the last business day of its fiscal year:
- (A) it has a public float of common equity of at least \$75 million, but less than \$700 million, computed as of the last business day of its most recently completed second fiscal quarter (i.e., June 30 for issuers with December 31 fiscal year ends);
 - (B) it has been subject to the reporting requirements of the Exchange Act for at least 12 calendar months;
 - (C) it has previously filed at least one annual report under the Exchange Act; and
 - (D) it is not eligible to use the requirements for smaller reporting companies in Regulation S-K for its annual and quarterly reports.
- (vi) Current Report: Form 8-K. Except as discussed in (G) and (H) below, a current report on Form 8-K must be filed with the SEC within four business days after the occurrence of a “triggering event.”

The “triggering events” are as follows:

- (A) Registrant’s Business and Operations:
 - (1) entry into a material definitive agreement;
 - (2) termination of a material definitive agreement; and
 - (3) bankruptcy or receivership.
- (B) Financial Information:
 - (1) completion of acquisition or disposition of assets;
 - (2) results of operations and financial condition (see (I) below);
 - (3) creation of a direct financial obligation or an obligation under an off-balance sheet arrangement of a registrant;
 - (4) triggering events that accelerate or increase a direct financial obligation or an obligation under an off-balance sheet arrangement;

- (5) costs associated with exit or disposal activities; and
 - (6) material impairments;
- (C) Securities and Trading Markets:
 - (1) notice of delisting or failure to satisfy a continued listing rule or standard; transfer of listing;
 - (2) unregistered sales of equity securities; and
 - (3) material modification to rights of security holders.
- (D) Matters Related to Accountants and Financial Statements:
 - (1) changes in registrant's certifying accountant; and
 - (2) non-reliance on previously issued financial statements or a related audit report or completed interim review.
- (E) Corporate Governance and Management:
 - (1) changes in control of registrant;
 - (2) departure of directors or certain officers; election of directors; appointment of certain officers; compensatory arrangements of certain officers;
 - (3) amendments to articles of incorporation or bylaws; change in fiscal year;
 - (4) temporary suspension of trading under registrant's employee benefit plans;
 - (5) amendments to the registrant's code of ethics, or waiver of a provision of the code of ethics;⁹⁴
 - (6) change in shell company status; and
 - (7) submission of matters to a vote of security holders.

⁹⁴ A U.S. issuer must disclose changes to, and waivers of, its code of ethics on Form 8-K or on the company's web site within 4 business days after the change or waiver. For a company to use its web site for this disclosure, it must have disclosed in its most recently filed annual report: (a) that it intends to disclose changes and waivers on its Internet web site, and (b) its web site address. See Chapter 10, at F.

- (F) Asset-Backed Securities:
- (1) ABS informational and computational material;
 - (2) change of servicer or trustee;
 - (3) change in credit enhancement or other external support;
 - (4) failure to make a required distribution; and
 - (5) Securities Act updating disclosure.

(G) Regulation FD Disclosure.

Unless filed under (H) (Other Events), a registrant must disclose under (G) (Regulation FD Disclosure) only information that it elects to disclose through Form 8-K pursuant to Regulation FD.

A registrant either furnishing a report on Form 8-K under (G) or electing to file a report on Form 8-K under (H) solely to satisfy its obligations under Regulation FD must furnish the report or make the filing, as applicable, in accordance with the requirements of Rule 100(a) of Regulation FD, including the deadline for furnishing or filing the report.

(H) Other Events.

The registrant may, at its option, disclose under (H) (Other Events) any events, with respect to which information is not otherwise called for by Form 8-K, that the registrant deems of importance to security holders. The registrant may, at its option, file a report under (H) disclosing the non-public information required to be disclosed by Regulation FD.

Although reports of “other events” are optional, issuers are encouraged to file “promptly” after the occurrence of the specific event.

(I) Financial Statements and Exhibits.

Companies must furnish publicly disclosed earnings releases to the SEC on Form 8-K if the information is not

otherwise disclosed by webcast or broadcast in accordance with the SEC's procedures.⁹⁵

(b) Smaller Reporting Companies.

Smaller reporting companies (including foreign companies) using U.S. issuer forms for Exchange Act registration and reporting (i.e., Forms 10, 10-K, 10-Q and 8-K) qualify for scaled disclosure requirements. Smaller reporting companies are not required to provide risk factor disclosure in Forms 10, 10-K and 10-Q. For further discussion of smaller reporting companies, see Chapters 4 and 12.

(c) Proxy Statement and Annual Report.

- (i) Proxy Statement. As a result of the issuer becoming a reporting company under the Exchange Act, any "solicitation" of a proxy is subject to the SEC's detailed proxy rules. No solicitation may be made by the issuer unless it is accompanied by a proxy statement that contains the information specified by Schedule 14A under the Exchange Act. Much of the information required to be disclosed is similar to that included in a registration statement, including information concerning directors or nominees for election as directors, executive compensation (although expanded as compared to the registration statement), security ownership of certain beneficial owners and management and related party transactions. The expanded information in the proxy statement includes a report by the compensation committee of the issuer's board of directors regarding the committee's compensation policies for the issuer's chief executive officer and other executive officers.

Regulation 14A under the Exchange Act also dictates the form of proxy to be used for a proxy solicitation.

⁹⁵ Under Item 2.02 of Form 8-K, if a registrant, or any person acting on its behalf, makes any public announcement or release (including any update of an earlier announcement or release) disclosing material non-public information regarding the registrant's results of operations or financial condition for a completed quarterly or annual fiscal period, the registrant must disclose the date of the announcement or release, briefly identify the announcement or release and include the text of that announcement or release as an exhibit.

However, a Form 8-K is not required to be furnished to the SEC under Item 2.02 in the case of disclosure of material non-public information that is disclosed orally, telephonically, by webcast, by broadcast or by similar means if: (a) the information is provided as part of a presentation that is complementary to, and initially occurs within 48 hours after, a related, written announcement or release that has been furnished on Form 8-K under Item 2.02 before the presentation; (b) the presentation is broadly accessible to the public by dial-in conference call, by webcast, by broadcast or by similar means; (c) the financial and other statistical information contained in the presentation is provided on the registrant's web site, together with any information that would be required under Regulation G; and (d) the presentation was announced by a widely disseminated press release that included instructions as to when and how to access the presentation and the location on the registrant's web site where the information would be available.

Generally, preliminary proxy materials must be filed with the SEC for review at least 10 calendar days before the materials will be mailed to shareholders. However, substantially more time should be allowed if the proxy materials cover a complex transaction. Filing with the SEC before mailing is not necessary if: (A) the proxy materials relate to a shareholders' meeting at which the only matters to be voted on are the election of directors, the selection of auditors, certain shareholder proposals or the approval or ratification of certain employee benefit plans or amendments; and (B) the matters to be voted on are not "contested." However, even if preliminary proxy materials need not be filed with the SEC, definitive proxy materials must be filed with the SEC when the materials are mailed to shareholders. While the SEC generally does not impose filing fees for proxy materials, it does impose fees for proxy materials relating to mergers and acquisitions. These fees vary depending upon the type and size of the transaction for which the solicitation is being made.

From time to time, the issuer may receive notices from shareholders that they intend to present proposals at a forthcoming meeting of shareholders. If the shareholders and their proposals meet certain requirements, the proposals must be included in the issuer's proxy statement unless the issuer is entitled to omit them under one of the provisions for doing so in the SEC's proxy rules. When such notices of shareholder proposals are received by the issuer, copies should be sent to counsel and a course of action for dealing with the proposal should be established. If the issuer plans to omit the proposal, it must file an explanation of its position with the SEC.

To ensure that the actual beneficial owners of the issuer's voting securities will receive the proxy materials, the issuer will need to ask the brokers, banks or other persons who are the "record holders" of the securities (i.e., holders of stock in "street name"): (A) whether they are the beneficial owners of the securities and, if not, how many copies of the proxy materials they will need to distribute to the beneficial owners of the stock held in the broker's, bank's or other record owner's name; (B) whether there are any agents designated by the record holders to distribute proxy materials; and (C) whether there are any beneficial owners who do not object to receiving materials directly. The issuer must request this information at least 20 business days before the record date for the shareholder vote. The request is generally made through the issuer's transfer agent.

In 2007, the SEC adopted a "notice and access" model for delivery of proxy materials (i.e., the SEC adopted amendments to the proxy

rules under the Exchange Act that provide an alternative method for issuers and other persons to furnish proxy materials to shareholders by posting them on an Internet web site and providing shareholders with notice of the Internet availability of the proxy materials). Specifically, the notice and access proxy rules: (A) require issuers and other soliciting persons to post their proxy materials on an Internet web site and provide a Notice of Internet Availability of Proxy Materials (notice) to shareholders; and (B) provide issuers and other soliciting persons with an option as to whether to send a full set of proxy materials to all shareholders (i.e., to furnish paper copies of the proxy materials along with the notice) or to send shareholders only the notice. If the issuer or other soliciting person chooses not to furnish a paper copy of the proxy materials along with the notice, a shareholder may request delivery of a copy at no charge to the shareholder. Thus, the notice and access proxy rules provide shareholders with the ability to choose the means by which they access proxy materials. While many issuers experienced significant cost savings using the notice-only option, statistics indicated lower shareholder response rates to proxy solicitations when the notice-only option was used. The SEC was concerned that some investors may have been confused when issuers and other soliciting persons distributed proxy materials using the notice-only option and believed its rules should be amended to provide additional flexibility for issuers and other soliciting persons to better communicate with shareholders to reduce that confusion.

Accordingly, in 2010, the SEC adopted amendments that give issuers and other soliciting persons additional flexibility to provide shareholders with a more effective explanation of the importance and effect of the notice and the reasons for its use. Specifically, the amendments: (A) provide additional flexibility concerning the format and content of the notice, and (B) permit issuers and other soliciting persons to better communicate with shareholders by including explanatory materials concerning the reasons for the use of the notice and access proxy rules and the process of receiving and reviewing proxy materials and voting under the notice and access proxy rules. The amendments also: (A) revise the time frame for delivering a notice to shareholders when a soliciting person other than the issuer relies on the notice-only option, and (B) permit mutual funds to accompany the notice with a summary prospectus.

- (ii) Annual Report to Shareholders. Before or together with the mailing to shareholders of the proxy materials for the annual meeting of shareholders, the issuer is required to provide to its shareholders an annual report (typically, the “glossy” report,

although, as discussed below, this report may consist of the Form 10-K with a “wrapper” around it that contains certain additional information). Issuers often use “puffier” public relations-type language in preparing “glossy” annual reports to shareholders. However, there is specific information required to be included in the annual report, which is substantially similar to the disclosure required in the Form 10-K. Instead of preparing an entirely new report, some issuers create a “wrapper” to go around their Form 10-K. The wrapper typically includes a letter to shareholders discussing the past year and any significant developments expected or hoped for in the coming year and such other information as the issuer deems suitable. Annual reports to shareholders must be mailed to the SEC no later than the date on which the report is first given or sent to security holders, but they are not considered to be “filed.” Consequently, they do not independently subject the issuer to Exchange Act liability, except where information is incorporated by reference into the Form 10-K. However, as with any communication issued by the Company, the annual report to shareholders can be a significant source of liability if it contains any material misstatements or omissions.

- (iii) Foreign Private Issuers Exempt. Foreign private issuers are exempt from proxy regulation under Section 14 of the Exchange Act.

3. Registration and Reporting Forms For Foreign Private Issuers and Canadian Issuers

A foreign private issuer that seeks to register securities and report annually under the Exchange Act has a choice of forms available to it for Exchange Act registration statements and annual reports. A foreign private issuer may use:

- (a) Form 20-F. The standard form for Exchange Act registration and annual reporting by foreign private issuers is Form 20-F, which is similar in content to Form 10-K.
- (b) Form 40-F. The MJDS form for Exchange Act registration and annual reporting by qualifying Canadian foreign private issuers is Form 40-F. This is a cover “wrapper” for Canadian annual information.
- (c) Form 8-A. The short form registration statement under the Exchange Act is Form 8-A, which may be used only with a public offering of the relevant class of securities under the Securities Act.
- (d) As an alternative to (a) or (b), a foreign private issuer may voluntarily comply with the reporting requirements for U.S. issuers described above.

4. Form 20-F Registration Statement and Annual Report

(a) Foreign private issuers registered under the Exchange Act, except Canadian issuers qualified to use the MJDS Form 40-F, must file with the SEC an annual report on Form 20-F: (i) within six months after the end of their fiscal year for fiscal years ending before December 15, 2011; and (ii) within four months after the end of their fiscal year for fiscal years ending on or after December 15, 2011. Form 20-F requires significant disclosure about the issuer's business and financial condition, but the detail required is less than that required under Form 10-K annual reports (and Form 10 registration statements) filed by U.S. issuers or non-U.S. issuers that do not qualify as foreign private issuers.

(b) Form 20-F Disclosure Requirements. In many respects, the textual requirements (i.e., the non-financial statement disclosure requirements) of Form 20-F are closely aligned with the international disclosure standards of the International Organization of Securities Commissions ("IOSCO"). Still, the SEC requires detailed disclosure of certain activities, such as activities in derivative securities and hedging.

Form 20-F disclosure includes, among other things, a description or discussion of the issuer's:

- (i) business and major properties;
- (ii) major legal proceedings or governmental proceedings;
- (iii) controlling (10%) shareholders;
- (iv) trading markets;
- (v) MD&A;
- (vi) tax issues;
- (vii) management and management compensation;
- (viii) material related party transactions;
- (ix) quantitative and qualitative disclosure about market risk; and
- (x) audited financial statements.

(c) Form 20-F Financial Statement Disclosure. Form 20-F (either as a registration statement or annual report) must contain audited consolidated statements of income and cash flow for the issuer's three most recently completed fiscal years and balance sheets as of the end of the three most recently completed fiscal years. However, a foreign issuer need not provide a balance sheet for the earliest of the three years if that balance sheet is not required by a jurisdiction outside the United States. Unaudited six-month financial statements must be included in Form 20-F registration statements (but not annual reports) if the registration

statement is filed more than nine months after the end of the last fiscal year for which audited statements are provided.

Financial statements included in a Form 20-F registration statement or annual report may be prepared under U.S. GAAP, IFRS or GAAP of an appropriate foreign country. If prepared other than under U.S. GAAP or IASB IFRS, the annual and interim financial statements included in the filing must be reconciled to U.S. GAAP under: (i) either Item 17 or Item 18 of Form 20-F for fiscal years ending before December 15, 2011; and (ii) Item 18 of Form 20-F for fiscal years ending on or after December 15, 2011. The reconciliation of the income statement of the earliest of the three fiscal years presented may be omitted if the information has not previously been included in an SEC filing. This normally occurs when Form 20-F is used as an Exchange Act registration statement.

(d) SEC Review. Registration statements under the Exchange Act on Form 20-F are reviewed by the SEC. Annual reports on Form 20-F are subject to SEC review, but generally are not reviewed unless incorporated by reference into Securities Act registration statements.

After a foreign private issuer files its preliminary Form 20-F with the SEC, the SEC staff usually takes at least 30 days to review and comment on it. Depending on the scope of the comments, it usually takes a few weeks to respond to the comments and clear the SEC process. At the end of the process, the registration statement is declared “effective” by the SEC. Normally, these filings become publicly available upon filing (except for exhibits or portions of them that have been granted confidential treatment). Generally, the SEC permits a foreign private issuer who has confidentiality concerns to submit once a preliminary Securities Act registration statement or Exchange Act registration statement (in this case, the Form 20-F) on a confidential basis. The Form 20-F would then not technically be “filed” with the SEC and would become publicly available only after the issuer had completed the SEC review process and made a formal filing. (Except in unusual circumstances, once a foreign private issuer has registered a transaction under the Securities Act or a class of securities under the Exchange Act, the SEC will not accept from that issuer additional registration statements on a draft basis and will not review or screen a registration statement until it is publicly filed. In recent years, the SEC rarely has granted exceptions to this policy.) There is no filing fee for the Form 20-F.

5. Form 40-F Registration Statement and Annual Report for Canadian Issuers

(a) Eligibility. Form 40-F may be used to register securities of certain “substantial” Canadian issuers under Section 12 of the Exchange Act or to file Exchange Act annual reports. These issuers generally must:

- (i) be incorporated or organized under the laws of Canada or any of its provinces or territories;
- (ii) be a foreign private issuer or a crown corporation;
- (iii) have been subject to the periodic reporting requirements of any securities commission or stock exchange in Canada for at least 12

calendar months and be in compliance with those requirements;
and

- (iv) have outstanding equity shares held by non-affiliates (i.e., generally, shareholders other than officers, directors and 10% shareholders) with an aggregate market value of at least \$75 million.

MJDS issuers test their eligibility to file reports on Form 40-F as of the end of their fiscal year.

(b) Information Required. Form 40-F consists largely of disclosure documents and other information that the issuer is required to prepare by the laws of its home jurisdiction or the Canadian securities exchange upon which its securities are listed. If filed as a registration statement under the Exchange Act, the form must include all information material to an investment decision that the issuer, since the beginning of its last full fiscal year:

- (i) made or was required to make public under the law of any Canadian jurisdiction;
- (ii) filed or was required to file with a stock exchange on which its securities are traded and which was made public by that exchange;
or
- (iii) distributed or was required to distribute to its security holders.

If the form is being filed as an annual report, it must include the annual information form required under Canadian law and the issuer's audited annual financial statements and accompanying management's discussion and analysis.

Consents of the auditors of the financial statements and of any other experts named in the filing (such as engineers named as having certified oil and gas or mineral reserve reports) must be filed as exhibits.

Financial statements included in documents included in the filing, other than interim financial statements, must be reconciled to U.S. GAAP as required by Item 17 of Form 20-F, unless:

- (i) the form is filed for investment grade debt or preferred stock eligible for registration on Form F-9, or
- (ii) the issuer is required to file reports under Section 15(d) of the Exchange Act solely as a result of having filed a registration statement on Form F-7, F-8, F-9 or F-80,

in which case no reconciliation to U.S. GAAP is required.

The SEC's rules on auditor independence, as codified in Section 600 of the Codification of Financial Reporting Policies, apply to auditor reports on all financial statements that are included in a registration statement or annual report on Form 40-F, except that those rules do not apply with respect to periods prior to the most recent fiscal year for which financial statements are included in a registration statement under the Securities Act filed by the issuer on Form F-8, F-9, F-10 or F-80 or under the Exchange Act filed by the issuer on Form 40-F. Notwithstanding the exception in the previous sentence, those rules do apply with respect to any periods prior to the most recent fiscal year if the issuer previously was required to file with the SEC a report or registration statement containing an audit report on financial statements for such prior periods as to which the SEC's rules on auditor independence applied.

(c) SEC Review. Form 40-F registration statements are not normally reviewed by the SEC.

6. Form 6-K Current Report

Issuers reporting on Form 20-F or Form 40-F must furnish current reports on Form 6-K. The information provided on Form 6-K consists of whatever information the issuer:

- (a) makes or is required to make public under the law of the jurisdiction of its domicile or in which it is incorporated or organized;
- (b) 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
- (c) distributes or is required to distribute to its security holders.

The information required to be furnished on Form 6-K for the three categories above is: (i) information that is material for the issuer and its subsidiaries concerning: changes in business; changes in management or control; acquisitions or dispositions of assets; bankruptcy or receivership; changes in the issuer's certifying accountants; the financial condition and results of operations; material legal proceedings; changes in securities or in the security for registered securities; defaults upon senior securities; material increases or decreases in the amount outstanding of securities or indebtedness; the results of the submission of matters to a vote of security holders; transactions with directors, officers or principal security holders; and the granting of options or payment of other compensation to directors or officers; and (ii) any other information that the issuer deems of material importance to security holders.

Generally, for non-U.S. issuers, including Canadian issuers, the information that must be furnished with Form 6-K includes: (i) press releases, (ii) reports and other information filed with local securities commissions and stock exchanges, and (iii) annual and other shareholder mailings.

The Form 6-K report must be furnished promptly after the material contained in the report is made public as described above.

Form 6-K does not require that the issuer's filings or reports take any particular form or disclose any particular information. The information and documents furnished

on Form 6-K are not deemed “filed” for purposes of liability under Section 18 of the Exchange Act, but general anti-fraud principles (i.e., Rule 10b-5) of U.S. law do apply. Normally, Form 6-K reports are simply a cover page that encloses the document or press release being submitted, but some issuers include explanatory narrative disclosure in Form 6-K reports.

7. Voluntary Use of U.S. Issuer Forms

A number of foreign issuers eligible to use the registration and reporting forms under the Exchange Act available to foreign private issuers (i.e., Form 40-F or Form 20-F and Form 6-K) voluntarily elect to file the more burdensome forms for U.S. issuers (e.g., Forms 10-K and 10-Q) in order to conform to disclosure formats familiar to U.S. securities analysts and institutional investors. This is particularly true of issuers with heavy U.S. market interest. (Canadian issuers frequently comply with the Ontario Securities Commission’s (“OSC’s”) annual information form requirements by filing their U.S. Form 10-Ks with the OSC.)

Foreign private issuers that voluntarily file on U.S. issuer forms may file financial statements prepared under home country GAAP and provide a reconciliation to U.S. GAAP under Item 18 of Form 20-F. Foreign private issuers that voluntarily file on U.S. issuer forms may file financial statements prepared under 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 U.S. issuer forms.

Issuers that are eligible to report on Form 40-F or Form 20-F do not become subject to the U.S. proxy rules under Section 14 or Section 16 insider reporting and short-swing profit recapture merely by electing to use Form 10-K.

8. EDGAR

Generally, foreign private issuers are required to file electronically using the SEC’s “EDGAR” system, as are U.S. issuers.

9. Rule 10b-17 Notice

Rule 10b-17 under the Exchange Act requires the issuer “of a class of securities publicly traded by the use of any means or instrumentality of interstate commerce or of the mails or of any facility of any national securities exchange” to send a notice to the Financial Industry Regulatory Authority (“FINRA”) 10 days before the record date for any of the following actions relating to that class of securities: (a) a dividend or other distribution in cash or in kind, except an ordinary interest payment on a debt security, but including a dividend or distribution of any security of the same or another issuer; (b) a stock split or reverse stock split; or (c) a rights or other subscription offering. (For a rights or other subscription offering, if such 10 days advance notice is not practical, the notice must be sent on or before the record date and in no event later than the effective date of the registration statement to which the offering relates.) FINRA utilizes a form entitled “10b-17 Report” for this purpose. The timely filing of this Report permits FINRA to set an “ex-dividend” date and to inform the market of these corporate events.

D. The U.S. Foreign Corrupt Practices Act

All reporting issuers are subject to certain provisions of the U.S. Foreign Corrupt Practices Act of 1977 (“FCPA”). In general, the FCPA:

- (a) imposes requirements for record-keeping and internal accounting controls to assure that transactions will be properly recorded in the issuer’s financial records; and
- (b) prohibits payments (other than payments to expedite or secure the performance of routine governmental action) to foreign government officials and others for the purpose of obtaining or maintaining business or influencing performance of official functions. Two safe harbors permit payments that are either: (i) lawful in the jurisdiction where made, or (ii) a reasonable and bona fide expenditure directly related to promoting products or services or to executing or performing a contract with a foreign government or agency.

An issuer with non-U.S. operations should take steps to assure itself that the activities of its agents and employees are consistent with the requirements of the FCPA.

E. General Disclosure Obligations

Under the U.S. securities laws there is no general rule that an issuer with securities registered under the Exchange Act must promptly disclose all material corporate developments. Nevertheless, in certain circumstances there is a duty to disclose corporate developments, such as:

- when an SEC filing is required (e.g., an annual report, quarterly report or current report);
- when required by the listing standards of the issuer’s trading market;
- when the issuer is buying or selling its own securities;
- when prior statements of the issuer were incorrect when made;⁹⁶ or
- when material non-public information has been selectively disclosed to a shareholder or market participant but not to the market as a whole.

It is not always clear whether one of the circumstances triggering disclosure has occurred. Consequently, whenever there has been a material corporate development, an issuer should consider whether to disclose the development promptly.

A policy of withholding material information, while permissible except in the circumstances outlined above, is not always advisable unless there is a bona fide corporate justification for doing so. The trend of the law, as well as the SEC’s enforcement position,

⁹⁶ A duty by a company to make public disclosure of important developments has also been recognized in some (but not all) instances where a company has made a previous public announcement that is still reasonably current and on which traders could reasonably rely, but which is no longer accurate because of subsequent developments.

favors full and fair disclosure. In most circumstances, as a matter of caution and good business practice, the issuer should disclose material events on a timely basis. There is also a fundamental investor relations concern. An issuer's failure to promptly disclose major developments (particularly adverse ones) could affect the willingness of securities analysts and investors to follow and believe in the issuer.

1. Trading Market Requirements

The NYSE and NASDAQ have independent disclosure requirements. An issuer is expected to quickly release to the public any information that might reasonably be expected to materially affect the market for its securities. However, neither the NYSE nor NASDAQ is likely to delist a company that does not make disclosure or takes a "no comment" position on a material development the rules require to be disclosed. An issuer may also wish to make prompt disclosure to correct unfounded rumors that result in unusual market activity or price variations. The NYSE and NASDAQ each require issuers to notify it of the release of any such information before its release to the public through the news media.

2. Purchases or Sales by an Issuer of Its Own Securities

If an issuer is buying or selling its own securities, it may have inside information. Generally, it is required to disclose material information under the general "disclose-or-abstain-from-trading" interpretation of the general anti-fraud rule, Rule 10b-5 under the Exchange Act. The SEC believes that an issuer should not be permitted to take advantage of others by buying or selling its securities when it knows of non-public material developments about its business. Consequently, if an issuer is buying or selling its own securities, it must disclose any non-public material developments about its business.

Many U.S. issuers have a formal policy that permits insiders to trade only during designated "window periods." Although not legally mandated, one common approach is for the window period to begin one week after filing of the annual or quarterly report under the Exchange Act or a current report on Form 8-K concerning financial results and to end after 10 to 30 days.

3. Misstatements, Corrections and Updating

If an issuer is permitted to be silent about a matter, but nonetheless choose to make statements, its statements must be truthful, complete and not misleading. For example, while an issuer may not be required to disclose preliminary merger negotiations, it should not deny that talks are occurring with a prospective merger partner. However, the issuer may take a "no-comment" position. If it does so, it should take this position consistently.

An issuer may also have a duty to disclose material developments that cause a prior statement of the issuer, on which investors are likely still to be relying, to become misleading. For example, if an issuer announced in September that it expected its earnings for the year to be better than those of the prior year, the issuer might well have to disclose if its year-end expectations materially changed as a result of developments in November. There are questions about how long the duty to update exists and whether the duty to update can be eliminated by a clear statement in an initial statement to the effect that the information disclosed

is as of the date of the statement and that the issuer does not undertake to update the information.

There is no duty to correct rumors or statements made by third parties without the issuer's involvement. However, it is often difficult to be confident that the source of a rumor is not someone at the issuer itself. Consequently, corrective action may sometimes be appropriate.

4. Timing of Disclosure

So long as there is no affirmative duty to disclose information immediately (i.e., (a) there is no current requirement for a periodic report to the SEC, (b) there is no requirement under NASDAQ or other stock exchange rules, (c) the issuer is not buying or selling its securities, (d) there is no statement of the issuer that needs to be corrected, and (e) there has been no selective disclosure), the timing of a particular disclosure is within an issuer's business judgment and disclosure may be deferred. Even where an issuer may otherwise have an affirmative duty to disclose information, disclosure may in some instances be delayed if the information is not yet "ripe" for disclosure, i.e., the information has not yet become definite enough to give management confidence in its accuracy and there is a risk that disclosure of the information would mislead investors or otherwise be premature. If an issuer expects to be required to disclose a matter in an SEC filing, the issuer frequently discloses it more promptly than legally required, by issuing a press release. Judgments in this area are very fact specific and can be very difficult.

Adequate public disclosure of material information is not accomplished by the simple release of the information. No trades should be made by one possessing material non-public information (including the issuer) until after there has been adequate dissemination of the information, and time for the market to react to the information. Thirty-six hours after the U.S. public announcement is a common period allowed for market reaction.

F. Deregistration from the Exchange Act Reporting System

1. Equity Securities

To deregister a class of equity securities, a foreign private issuer must meet: (a) each of three general conditions set forth below; and (b) either: (i) the trading volume threshold, or (ii) one of the 300-holder thresholds.

(a) General Conditions

(i) Prior Exchange Act Reporting Condition. The foreign private issuer must have:

(A) been an Exchange Act reporting company for at least 12 months before the deregistration;

(B) filed or furnished all reports required for this period; and

- (C) filed at least one annual report on Form 20-F (or Form 40-F), or a special financial report (filed with the SEC under Rule 15d-2 under the Exchange Act).
- (ii) Home Country Listing Condition. For the preceding year, the issuer must have listed the subject class of securities on one or more exchanges in a non-U.S. jurisdiction that, either alone or together with the trading in one other non-U.S. jurisdiction, constitutes the primary trading market for the securities (one or two markets constituting 55% of worldwide trading).
- (iii) One Year Dormancy Condition. The issuer must not have sold its securities in the United States in a registered offering during the preceding 12 months, except for certain minor registered securities offerings, i.e., registered offerings for securities that are issued:
 - (A) to the issuer's employees;
 - (B) by selling security holders in non-underwritten offerings;
 - (C) upon the exercise of outstanding rights granted by the issuer if the rights have been granted pro rata to all existing security holders of the relevant class (except when issued in a standby underwritten offering or other similar arrangement in the United States);
 - (D) under a dividend or interest reinvestment plan (except when issued in a standby underwritten offering or other similar arrangement in the United States); or
 - (E) upon the conversion of outstanding convertible securities or upon the exercise of outstanding transferable warrants issued by the issuer (except when issued in a standby underwritten offering or other similar arrangement in the United States).

(b) Alternative Exit Thresholds

- (i) (A) Trading Volume Threshold. The U.S. average daily trading volume ("ADTV") of the relevant class of equity securities for a recent 12-month period (that ended no more than 60 days before the filing of the deregistration form) must be no greater than 5% of the ADTV of that class of securities worldwide for the same period.
- (B) One Year Ineligibility Period After Delisting or Termination of ADR Facility. A foreign private issuer that has delisted (voluntarily or involuntarily) a class of equity

securities from a U.S. national securities exchange or automated inter-dealer quotation system or terminated its sponsored ADR program for a class of equity securities must wait at least one year from the date of the delisting or termination of the ADR program before it may file the deregistration form to deregister a class of equity securities.

(C) The Requirement To Wait One Year Does Not Apply If:

- (1) when the issuer delisted the relevant class of equity securities, the U.S. ADTV of that class of securities did not exceed 5% of the worldwide ADTV of that class of securities for the preceding 12 months;
- (2) when the issuer terminated its ADR program, the U.S. ADTV of the ADRs did not exceed 5% of the worldwide ADTV of the underlying class of securities for the preceding 12 months; or
- (3) the issuer delisted the relevant class of equity securities or terminated its ADR program before March 21, 2007.

(ii) 300 Holder Threshold. Alternatively, a foreign private issuer may deregister a class of equity securities if, on a date within 120 days before the filing of the deregistration form, that class of equity securities was held of record either by:

- (A) fewer than 300 persons worldwide; or
- (B) fewer than 300 persons resident in the United States.

A foreign private issuer that deregisters equity securities under this rule (i.e., Rule 12h-6 under the Exchange Act) will automatically receive the exemption under Rule 12g3-2(b). Absent that exemption, a foreign private issuer deregistering under Rule 12h-6 would have to re-register its equity securities under Section 12(g) of the Exchange Act if, as of a financial year-end after the deregistration, it had 500 or more shareholders of record worldwide (300 or more of which were U.S. residents) and more than \$10 million in assets.

2. Successor Issuer Status - Effect on M&A Transactions

A foreign private issuer that, after a business combination where shares are used as consideration for the purchase price, has succeeded to the U.S. registration or reporting obligations of another issuer will be able to assume the reporting history of the acquired company and deregister immediately after that acquisition if:

- (a) the acquired company has met the prior Exchange Act reporting condition;
- and

- (b) the acquiror meets the other deregistration conditions.

Consequently, if a foreign private issuer that is not an Exchange Act reporting company acquires a company that is an Exchange Act reporting company and uses its own shares as consideration in the acquisition, the acquiror will be able to deregister without regard to the trading volume of the acquired company because only the acquiror's trading volume will be relevant for meeting the trading volume threshold and the home country listing condition.

However, if the acquiror's shares issued in a business combination must be registered under the Securities Act, the one year dormancy condition will still have to be met. Consequently, the ability to use the reporting history of the acquired company will only be useful in M&A transactions where the shares that are issued as consideration for the purchase price are exempt from registration under the Securities Act (e.g., under Rule 802 or Section 3(a)(10)).

3. Debt Securities

To deregister a class of debt securities, a foreign private issuer must:

- (a) have submitted all required Exchange Act filings, including at least one Exchange Act annual report, since the debt securities were registered under the Exchange Act; and
- (b) have less than 300 record holders worldwide or that are residents of the United States, in either case on a date within 120 days before filing for deregistration.

CHAPTER 10.

FEDERAL CORPORATE GOVERNANCE STANDARDS: SARBANES-OXLEY AND NYSE AND NASDAQ LISTING STANDARDS

A. Introduction

The Sarbanes-Oxley Act of 2002 (“SOX”) is the most important securities legislation since the New Deal. The Act contains 76 civil and criminal sections and runs almost 70 pages. The net effect of SOX’s provisions affecting public companies was to create a new set of minimum federal corporate governance standards.

Most of the provisions of SOX that affect board structure and function were implemented through SEC rulemaking and are enforced directly by the SEC. Other provisions were implemented through the listing standards of the New York Stock Exchange (“NYSE”) and the NASDAQ Stock Market (“NASDAQ”). The NYSE and NASDAQ each submitted to the SEC a set of corporate governance standards for inclusion in its listing requirements. Together, this latticework of statute, SEC rules and listing standards created new federal corporate governance standards.

Generally, SOX applies to all companies (i.e., those organized within the United States or outside the United States) that have registered equity or debt securities with the SEC under the Exchange Act, including non-U.S. reporting companies. However, some provisions, including those for independence of audit committee members, apply only to companies that have securities listed on an exchange (including NASDAQ). Most provisions of SOX also apply to companies that have registered a public offering of their securities in the United States or that have filed a registration statement under the Securities Act that has not yet become effective. In those cases, compliance may be required only during the period when they have a reporting obligation, which will continue at least until the fiscal year of the company following the fiscal year in which it registered its offering. But, a foreign private issuer that has not sold securities to the public in the United States, or that is exempt from Exchange Act registration under Rule 12g3-2(b) under the Exchange Act, is not subject to SOX.

For foreign issuers, NYSE and NASDAQ corporate governance standards continue to defer to home country practices in most instances. However, foreign issuers: (a) are required to comply with most of the audit committee requirements, and (b) are required to disclose any significant ways in which their corporate governance practices differ from those required by the listing standards.

These corporate governance standards are in addition to, and do not change, existing fiduciary duties of directors. Generally, these duties under state laws prescribe fiduciary duties of care and loyalty. The “duty of care” requires directors to act with reasonable care and good faith in fulfilling their duties. The “business judgment rule” protects directors from liability under the duty of care when they act in good faith, without self-interest and diligently. The “duty of loyalty” requires directors to act in the best interests of the company and all its shareholders and not in their own self interest. The current climate may affect judicial interpretation of these traditional standards, including the business judgment rule.

B. The Board of Directors

SOX and the SEC implementing rules do not address the role and authority of independent directors, except for audit committee activities.

Under NYSE and NASDAQ listing requirements, a majority of the board must be independent directors. Exemptions from this requirement are provided for controlled companies (i.e., where more than 50% of the voting power for the election of directors is held by an individual, a group or another company). Non-management directors must meet in regularly scheduled executive sessions without management. And, generally, listed companies must have: (a) an audit committee, (b) a compensation committee, and (c) a nominating and corporate governance committee, each comprised entirely of independent directors, unless under NASDAQ rules, independent directors as a group have the authority of the latter two committees.

A NYSE listed company can meet the requirement that listed companies hold regular meetings of non-management directors by holding regular executive sessions of independent directors. If a NYSE listed company chooses to hold regular meetings of all non-management directors, the company should hold an executive session including only independent directors at least annually. Also, all interested parties (i.e., not just shareholders) must be able to communicate their concerns about the NYSE listed company to the presiding director, or the non-management or independent directors as a group.

Because SEC rules permit companies to test their “foreign private issuer” status annually, at the end of their second fiscal quarter, NYSE listed issuers that no longer qualify as foreign private issuers at the end of their second fiscal quarter have until the end of that fiscal year to meet the NYSE’s board and committee independence requirements for U.S. companies.

C. Director Independence Criteria

SOX addresses a director’s “independence” only for the audit committee and focuses on only two criteria – the acceptance of compensatory fees from the company or any subsidiary (other than for serving as a director) and whether or not the director is an “affiliated person” of the company.

For a director to be “independent” under the NYSE listing requirements, the board must affirmatively determine that the director has no “material relationship” with the company “either directly or as a partner, shareholder or officer of an organization that has a relationship with the company.” Various specific relationships disqualify a person from being considered independent, and a three-year “look back” period is used in applying the independence criteria.

The NYSE does not view ownership of even a significant amount of stock, by itself, as a bar to an independence finding, because the concern is independence from management. However, shareholding will be relevant to determine a person’s status as an “affiliated person” under the independence requirement of SOX for audit committee membership. The basis for a board’s determination that a relationship between a company and a director is not material must be disclosed in the company’s proxy statement or, if the company does not file a proxy statement, in its annual report.

Under NASDAQ listing requirements, an “independent director” must have no relationship that would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. An “independent director” means a person who is not an executive officer or employee of the company or of any of its parents or subsidiaries or any other individual having a relationship that, in the opinion of the board of directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. Additionally, the board has an affirmative responsibility to determine that a director does not have any relationship that disqualifies him from being independent. Various specified relationships disqualify a person from being considered independent and a three-year “look back” period is used. NASDAQ does not believe that ownership of company stock by itself would preclude a board finding of independence.

D. The Audit Committee

1. Minimum Listing Standards for Audit Committees

As required by SOX, the SEC adopted Rule 10A-3 under the Exchange Act, which required all U.S. stock exchanges (including NASDAQ) to adopt listing standards requiring compliance with the following requirements:

(a) Audit Committee Member Independence. Every member of the audit committee of a listed company must be “independent.” To be independent, a director may not have accepted any direct or indirect compensatory fee from the company or its subsidiaries, other than compensation for service as a director or a committee member, and may not be an affiliated person of the company or of any of its subsidiaries. (For years, the NYSE and NASDAQ have each required all listed companies to have an audit committee, composed of at least three members, all of whom must be independent. The independence standards discussed above will apply for this purpose. However, under the NASDAQ rules, an audit committee member may temporarily not meet the independence standards if the board, under “exceptional and limited circumstances,” determines that membership on the committee by the individual is required by the best interests of the company and its shareholders. A company, other than a foreign private issuer, that relies on this exception must comply with the disclosure requirements set forth in Item 407(d)(2) of Regulation S-K. A foreign private issuer that relies on this exception must disclose in its next annual report (e.g., Form 20-F or 40-F) the nature of the relationship that makes the individual not independent and the reasons for the board’s determination.

(b) Auditor Selection and Oversight. The audit committee must have authority over, and be made “directly responsible” for, appointing, compensating and retaining the company’s independent auditor and for overseeing the work of the auditor in preparing or issuing any audit report (and any related work), including resolving any disagreements between management and the auditor regarding financial reporting. The auditor must report directly to the audit committee.

(c) Accounting Complaint Procedures. The audit committee must establish procedures for receiving, retaining and treating complaints about accounting, internal accounting controls or auditing matters and for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.

(d) Authority to Engage Advisers. The audit committee must have the authority to engage independent counsel and other advisers as the committee determines necessary to carry out its duties.

(e) Authority over Funding of Audits and Compensation of Audit Committee Advisers. The listed company must provide appropriate funding, as determined by the audit committee, for the compensation of: (i) the audit work and any related work of the company's independent auditor; (ii) any other audit, review or attest services provided to the company by a public accounting firm; and (iii) any advisers engaged by the audit committee. Additionally, the listed company must provide appropriate funding, as determined by the audit committee, for payment of ordinary administrative expenses of the audit committee that are necessary or appropriate in carrying out its duties.

These are minimum standards for listing and the exchanges are permitted to establish other standards for audit committees and other corporate governance matters that exceed these requirements.

2. Approval of Audit Engagements and of Non-Audit Services to be Provided by an Auditor

SOX requires for all reporting issuers (even if none of the company's securities are listed on an exchange) that the audit committee (or one or more designated members of the audit committee who are independent directors of the board of directors) approve all audit services and, subject to a de minimis exception, all permitted non-audit services, to be provided by the auditor or its associated persons, before the services are provided. "Audit services" include the provision of a comfort letter for a securities offering.

3. Required Reports to the Audit Committee

SOX and Rule 2-07 of Regulation S-X require for all reporting companies (except asset-backed issuers and certain registered investment companies) that the auditor report to the audit committee on a timely basis: (a) all critical accounting policies and practices used in the company's audited financial statements; (b) all alternative treatments of financial information within GAAP for policies and practices related to material items that have been discussed with management of the issuer, including: (i) the ramifications of the use of such alternative disclosures and treatments, and (ii) the treatment preferred by the auditor; (c) other material written communications between the auditor and the company's management, such as any management letter or schedule of unadjusted differences; and (d) if the audit client is an investment company, all non-audit services provided to any entity in an investment company complex that were not pre-approved by the registered investment company's audit committee under Rule 2-01(c)(7) of Regulation S-X.

4. Audit Committee Financial Expert Disclosure

All companies whose securities trade in the United States (even if none of the company's securities are listed on an exchange) must disclose in their annual reports whether or not the audit committee includes at least one member who is a "financial expert" (and, if not, the

reasons why not), subject to certain exceptions. An “audit committee financial expert” is a person who, as a result of

- (a) education and experience as a principal financial officer, principal accounting officer, controller, public accountant or auditor or experience in one or more positions that involve the performance of similar functions,
- (b) experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor or person performing similar functions,
- (c) experience overseeing or assessing the performance of companies or public accountants for the preparation, auditing or evaluation of financial statements, or
- (d) other relevant experience,

has: (i) an understanding of GAAP and financial statements; (ii) the ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves; (iii) experience in preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant’s financial statements, or experience in actively supervising one or more persons engaged in such activities; (iv) an understanding of “internal control over financial reporting” (defined in Chapter 12); and (v) an understanding of audit committee functions.

5. Attorney Reports of Material Violations

Under the SEC’s attorney conduct rules, an attorney representing a public company must report to the company’s audit committee evidence of material violations of the securities laws, breaches of fiduciary duty and similar violations of which the attorney becomes aware if, after reporting the evidence to the company’s chief legal officer (or to both the company’s chief legal officer and chief executive officer), the company has not provided an appropriate response to the report within a reasonable time. If the company does not have an audit committee, the attorney must report instead to: (a) another committee of the company’s board of directors comprised solely of independent directors; or (b) if the company does not have a committee comprised solely of independent directors, to the full board of directors.

As an alternative to reporting the evidence to the company's chief legal officer (or to both the company's chief legal officer and chief executive officer), the attorney may report the evidence to a qualified legal compliance committee, if the company has previously formed such a committee. By making such a report, the attorney has entirely satisfied his reporting obligation and is not required to assess the company's (or its qualified legal compliance committee's) response to the report. Therefore, by establishing a qualified legal compliance committee, a company can avoid having to satisfy its attorney as to the appropriateness and the adequacy of the company's response to reports of evidence of a material violation.

6. NYSE and NASDAQ Listing Standards Not Required by SOX

(a) Audit Committee Membership Financial Literacy and Financial Expertise. Under the NYSE listing requirements, all audit committee members must be "financially literate," as determined by the board, or must become financially literate within a reasonable period of time after their appointment. Additionally, at least one member of the committee (who need not be the committee chair) must have "accounting or related financial management expertise." A board may presume that a person who would be considered an audit committee financial expert under SOX has accounting or related financial management expertise.

Under the NASDAQ listing requirements, the audit committee members must be able to read and understand fundamental financial statements (including a company's balance sheet, income statement and cash flow statement) at the time of appointment. Additionally, at least one member of the committee must have past employment experience in finance or accounting, requisite professional certification in accounting or any other comparable experience or background that results in the individual's financial sophistication, such as being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities. An audit committee member cannot have participated in the preparation of the company's, or any of its current subsidiaries', financial statements during the past three years.

(b) Code of Ethics for Senior Financial Officers and Chief Executive Officers. The audit committee is often given the responsibility of ensuring compliance with the company's code of ethics.

(c) Audit Committee Responsibilities/Charter. Both the NYSE and NASDAQ require an audit committee charter, which must be in writing and specify the committee's purpose and responsibilities. A NYSE listed company (other than a closed-end fund) must make its audit committee charter available on its web site. A NYSE listed company must disclose in its annual proxy statement or, if it does not file an annual proxy statement, in its annual report on Form 10-K filed with the SEC that its audit committee charter is available on its web site and provide the web site address.

(d) Related Party/Conflict of Interest Transactions. The NYSE states that "related party transactions" normally include transactions between officers, directors, and principal shareholders and the company. Under NYSE listing requirements, each related party transaction must be reviewed and evaluated by an appropriate group within the listed company. While the NYSE does not specify who should review related party transactions, it believes that

the audit committee or another comparable body “might be considered as an appropriate forum for this task.” After the review, the company should determine whether or not a particular relationship serves the best interest of the company and its shareholders and whether the relationship should be continued or eliminated.

Under NASDAQ’s listing requirements all related party transactions must be approved by the audit committee (or another independent body of the board) as part of the company’s obligation to conduct “an appropriate review and oversight of all related party transactions for potential conflict of interest situations on an ongoing basis.” For this NASDAQ rule, “related party transactions” refers to transactions required to be disclosed under Item 404 of Regulation S-K (for U.S. issuers) or Item 7.B of Form 20-F (for non-U.S. issuers).

(e) Internal Audit. Under NYSE listing requirements, every company must have an internal audit function which will be overseen by the audit committee.

(f) Serving on More Than One Audit Committee. Under NYSE listing requirements, an audit committee member cannot serve simultaneously on more than three audit committees unless the board: (i) determines that the simultaneous service would not impair the ability of that person to effectively serve on the listed company’s audit committee; and (ii) discloses that determination either on the listed company’s web site or in its annual proxy statement (or, if the listed company does not file an annual proxy statement, in its annual report on Form 10-K filed with the SEC). If this disclosure is made on the listed company’s web site, the listed company must disclose that fact in its annual proxy statement or annual report, as applicable, and provide the web site address.

E. Other Board Committees

SOX does not address the role or composition of board committees, other than the audit committee. Under NYSE listing requirements, the nominating/corporate governance committee and the compensation committee must each be comprised entirely of independent directors and have a written charter that addresses: (a) the committee’s purpose and responsibilities, and (b) an annual performance evaluation of that committee. The responsibilities of the nominating/corporate governance committee, at a minimum, must be to: (a) identify individuals qualified to become board members, consistent with criteria approved by the board, and to select, or to recommend that the board select, the director nominees for the next annual meeting of shareholders; (b) develop and recommend to the board a set of corporate governance guidelines applicable to the corporation; and (c) oversee the evaluation of the board and management. The responsibilities of the compensation committee, at a minimum, must be to have direct responsibility to: (a) review and approve corporate goals and objectives relevant to chief executive officer (“CEO”) compensation, evaluate the CEO’s performance in light of those goals and objectives, and, either as a committee or together with the other independent directors (as directed by the board), determine and approve the CEO’s compensation level based on this evaluation; (b) make recommendations to the board concerning non-CEO executive officer compensation, and incentive-compensation and equity-based plans that are subject to board approval; and (c) prepare the disclosure required by Item 407(e)(5) of Regulation S-K. Boards may allocate the responsibilities of the nominating/corporate governance committee or the compensation committee to committees of their own denomination, provided that the committees

are comprised entirely of independent directors. Any such committee must have a committee charter.

A NYSE listed company must make its nominating/corporate governance committee charter and its compensation committee charter available on its web site. If any function of the nominating/corporate governance committee or the compensation committee has been delegated to another committee, the charter of that committee must also be made available on the listed company's web site. A NYSE listed company must disclose in its annual proxy statement or, if it does not file an annual proxy statement, in its annual report on Form 10-K filed with the SEC that its nominating/corporate governance committee charter and compensation committee charter are available on its web site and provide the web site address.

Under NASDAQ listing requirements, director nominees must be selected, or recommended for the board's selection, either by: (a) a nominations committee comprised solely of independent directors, or (b) independent directors constituting a majority of the board's independent directors in a vote in which only independent directors participate. Notwithstanding (a) above, if the nominations committee is comprised of at least three members, one director who is not independent and is not a current officer or employee or a family member of an officer or employee, may be temporarily appointed to the nominations committee if the board, under "exceptional and limited circumstances," determines that such individual's membership on the committee is required by the best interests of the company and its shareholders. A company that relies on this exception must disclose either on its web site or in the proxy statement for the next annual meeting after that determination (or, if the company does not file a proxy statement, in its Form 10-K or 20-F), the nature of the relationship that makes the individual not independent and the reasons for the determination. Additionally, the company must provide any disclosure required by Instruction 1 to Item 407(a) of Regulation S-K regarding its reliance on this exception. The NASDAQ listing requirements do not require a corporate governance committee. Under NASDAQ listing requirements, compensation of the CEO and of all other executive officers of the company must be determined, or recommended to the board for determination, either by: (a) a compensation committee comprised solely of independent directors, or (b) independent directors constituting a majority of the board's independent directors in a vote in which only independent directors participate. (Regarding CEO compensation, the CEO may not be present during voting or deliberations.) Notwithstanding (a) above, if the compensation committee is comprised of at least three members, one director who is not independent and is not a current officer or employee or a family member of an officer or employee, may be temporarily appointed to the compensation committee if the board, under "exceptional and limited circumstances," determines that such individual's membership on the committee is required by the best interests of the company and its shareholders. A company that relies on this exception must disclose either on its web site or in the proxy statement for the next annual meeting after that determination (or, if the company does not file a proxy statement, in its Form 10-K or 20-F), the nature of the relationship that makes the individual not independent and the reasons for the determination. Additionally, the company must provide any disclosure required by Instruction 1 to Item 407(a) of Regulation S-K regarding its reliance on this exception.

F. Codes of Ethics: Governance Guidelines

Under SOX and the SEC's implementing rules reporting companies (subject to certain

exceptions) are required to disclose in their annual reports whether they have adopted a code of ethics that applies to their principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions (and, if not, why not). The company must: (a) file with the SEC a copy of such code of ethics as an exhibit to its annual report; (b) post the text of such code of ethics on its Internet web site and disclose, in its annual report, its Internet address and the fact that it has posted such code of ethics on its Internet web site; or (c) undertake in its annual report filed with the SEC to provide to any person without charge, upon request, a copy of such code of ethics and explain the manner in which such request may be made. (As defined in the SEC rules, a “code of ethics” means written standards that are reasonably designed to deter wrongdoing and to promote: (a) honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships; (b) full, fair, accurate, timely, and understandable disclosure in reports and documents that an issuer files with, or submits to, the SEC and in the issuer’s other public communications; (c) compliance with governmental laws, rules, and regulations; (d) the prompt internal reporting of violations of the code to an appropriate person identified in the code; and (e) accountability for adherence to the code.) Additionally, the company must promptly disclose any change in, or waiver of, the code of ethics. Specifically, for U.S. issuers, the disclosure of a change or waiver must be made either on a Form 8-K or on the issuer’s web site. The Form 8-K must briefly describe the date and nature of the change or waiver, and for a waiver, the name of the person who received the waiver. The Form 8-K must be filed within four business days after the change or waiver. For an issuer to use its web site for this disclosure, it must have disclosed in its most recently filed annual report: (a) that it intends to disclose changes and waivers on its Internet web site, and (b) its web site address. The issuer must post the disclosure on its web site within the same four-business day time period required for Form 8-K filings, and the information must remain on the web site for at least one year. As discussed earlier, for foreign private issuers, current information is furnished under Form 6-K, instead of Form 8-K, but only to the extent required to be disclosed or filed under home country rules and practices. Consequently, a foreign private issuer must annually, in its annual report on Form 20-F or 40-F, briefly describe the nature of any change in, or waiver of, its code of ethics made during its most recently completed fiscal year that concerns the specified officers. The issuer must also file any change as an exhibit to the annual report. For a waiver, a foreign private issuer must also disclose the name of the person who received the waiver and the date of the waiver. The SEC strongly encourages foreign private issuers to voluntarily furnish a Form 6-K or use their web sites to promptly disclose changes or waivers. If disclosure is made by Form 6-K or web site posting within four business days after the change or waiver and otherwise meets the requirements for web site posting by U.S. issuers, no additional disclosure need be included in the annual report. While the SEC rules do not explicitly require board oversight of the code of ethics, given the seniority of the officers involved and the subject matter, responsibility to adopt and oversee the code will usually be a board responsibility, which, given the customary audit committee charter, may fall within the audit committee’s responsibilities.

Under NYSE listing requirements, a listed company must: (a) adopt and disclose a “code of business conduct and ethics” (i.e., a code of ethics) for directors, officers and employees, and (b) promptly disclose any waivers of the code for directors or executive officers. The code of ethics must require that any waiver of the code for executive officers or directors may be made only by the board or a board committee. Additionally, the code of ethics must contain compliance standards and procedures that will facilitate the effective operation of the code.

These standards should ensure prompt and consistent action against violations of the code. The code of ethics should discuss conflicts of interest, corporate opportunities, confidentiality, fair dealing, protection and proper use of company assets, compliance with laws, rules, and regulations (including insider trading laws), and the reporting of illegal or unethical behavior. A listed company must make its code of ethics available on its web site. Additionally, a listed company must disclose in its annual proxy statement or, if it does not file an annual proxy statement, in its annual report on Form 10-K filed with the SEC that its code of ethics is available on its web site and provide the web site address. To the extent that a listed company's board or a board committee determines to grant a waiver of the code for an executive officer or director, the waiver must be disclosed to shareholders within four business days of the determination. Disclosure must be made by distributing a press release, providing web site disclosure, or by filing a current report on Form 8-K with the SEC.

Under NASDAQ listing requirements, the listed company must adopt a "code of conduct" applicable to all directors, officers and employees, which must be publicly available. This code of conduct must comply with the definition of a "code of ethics" set out in SOX and the SEC's implementing rules. Additionally, the code must provide for an enforcement mechanism to ensure that the code is implemented properly and consistently. Any waivers of the code for directors or executive officers must be approved by the company's board of directors. Companies other than foreign private issuers must disclose such waivers within four business days by filing a current report on Form 8-K with the SEC or, in cases where a Form 8-K is not required, by distributing a press release. Foreign private issuers must disclose such waivers either by distributing a press release or including disclosure in a Form 6-K or in the next Form 20-F or 40-F. Alternatively, a company, including a foreign private issuer, may disclose waivers on its web site in a manner that meets the requirements of Item 5.05(c) of Form 8-K.

G. Other SOX Standards Applicable to Directors or Officers

1. **Prohibition on Personal Loans.** Companies are prohibited from extending or maintaining credit, arranging for the extension of credit, or renewing an extension of credit, in the form of a personal loan to or for any director or executive officer (or equivalent) of the company other than certain consumer credit arrangements (such as home improvement or credit card loans) made in the ordinary course of business, of a type generally made available by the company to the public and on market terms no more favorable than those offered by the company to the general public. (Companies that are or own broker-dealers may make margin loans to employees, unless used to carry stock of the company.) Personal loans in existence on July 30, 2002 may continue in effect, provided there is no material modification to any term or any renewal. Additionally, SOX's prohibition on personal loans does not apply to any loan made (or maintained) by a Federal Deposit Insurance Corporation (FDIC)-insured bank or savings association if the loan is subject to the insider lending restrictions of Section 22(h) of the Federal Reserve Act. This exemption does not apply to non-U.S. banks because they are not FDIC-insured. However, the SEC has adopted Rule 13k-1 under the Exchange Act, which remedies this disparate treatment of foreign banks by exempting from SOX's insider lending prohibition those foreign banks that meet specified criteria similar to those that qualify U.S. banks for the statutory exemption.

2. No Interference With Auditor. No action may be taken by any director or officer of the company (or other person acting under the direction thereof) to fraudulently influence, coerce, manipulate or mislead any independent auditor of the company's financial statements for the purpose of rendering the financial statements materially misleading.

3. Reporting of Trading in Company Equity Securities. Officers, directors and beneficial owners of 10% or more of a class of equity securities registered under the Exchange Act of a U.S. company must file with the SEC a statement of their ownership of the company's equity securities under Section 16 of the Exchange Act, effectively disclosing their purchases or sales on an accelerated basis, generally within two business days of the trade or other event requiring the filing. Section 16 of the Exchange Act is discussed further in the next Chapter.

4. Bar to Future Service. Any person found to have violated the general anti-fraud provision of the Securities Act (Section 17(a)(1) of that Act) or the Exchange Act (Section 10(b) of that Act), or related SEC rules, can be barred by a court or the SEC, after notice and a hearing, from serving as a director or officer of a public company if his conduct demonstrates "unfitness" to serve as a director or officer of such a company. The bar may be subject to conditions or unconditional, and it may be permanent or temporary.

H. Shareholder Approval Requirements

Voting on Equity Compensation Plans. Under NYSE listing requirements, shareholders must be given the opportunity to vote to approve or disapprove all equity compensation plans and any material revisions to the terms of such plans, except for: (a) employment inducement awards; (b) certain grants, plans and amendments in the context of mergers and acquisitions (see below); and (c) tax-qualified plans, such as ESOPs and 401(k) plans; brokers may only vote customer shares on proposals for such plans on customer instructions. There are two exemptions from the shareholder approval requirement for mergers and acquisitions. First, shareholder approval is not required to convert, replace or adjust outstanding options or other equity compensation awards to reflect the transaction. Second, shares available under certain plans acquired in acquisitions and mergers may be used for certain post-transaction grants without further shareholder approval. This exemption applies to situations where a party that is not a listed company after the transaction has shares available for grant under pre-existing plans that were previously approved by shareholders. A plan adopted in contemplation of the merger or acquisition transaction would not be considered "pre-existing" for this exemption.

Under NASDAQ listing requirements, shareholder approval is required before issuing securities when a stock option or purchase plan is to be established or materially amended or other equity compensation arrangement made or materially amended, under which stock may be acquired by officers, directors, employees or consultants, except for: (a) warrants or rights issued generally to all security holders of the company or stock purchase plans available on equal terms to all security holders of the company (such as a typical dividend reinvestment plan); (b) tax qualified, non-discriminatory employee benefit plans (e.g., plans that meet the requirements of Section 401(a) or 423 of the Internal Revenue Code) or parallel nonqualified plans, if such plans are approved by the company's independent compensation committee or a majority of the company's independent directors; (c) plans that merely provide a convenient way to purchase shares on the open market or from the company at fair market value; (d) plans or arrangements

involving a merger or acquisition, in the two situations discussed above; and (e) issuances to a person not previously an employee or director of the company, or following a bona fide period of non-employment, as an inducement material to the individual's entering into employment with the company, if such issuances are approved by the company's independent compensation committee or a majority of the company's independent directors. Promptly after any employment inducement grant made in reliance on this exception, the company must disclose in a press release the material terms of the grant, including the recipient(s) of the grant and the number of shares involved.

I. Education and Training of Directors

SOX does not address the education and training of directors.

Under NYSE listing requirements, listed companies' corporate governance guidelines are required to address director orientation and continuing education. The NYSE and the NYSE Foundation support a number of programs that offer continuing education to directors and other executives of publicly traded companies.

NASDAQ will make available to directors of listed companies relevant continuing education opportunities concerning governance responsibilities.

J. Certification and Notification

In addition to the well-known SOX certifications, the NYSE requires a listed company's chief executive officer to certify annually to the NYSE that he is not aware of any violation by the listed company of NYSE corporate governance listing standards, qualifying the certification to the extent necessary. The NYSE also requires the company to file an interim certification with the NYSE each time a change occurs in the composition of the company's board of directors or any of the board committees subject to NYSE corporate governance listing standards. The chief executive officer must promptly notify the NYSE in writing after any executive officer of the listed company becomes aware of any non-compliance with NYSE corporate governance listing standards.

Under NASDAQ listing requirements, a listed company must promptly notify NASDAQ after an executive officer of the company becomes aware of any non-compliance by the company with NASDAQ corporate governance listing standards.

Additionally, if a U.S. company has notified a national securities exchange that maintains the principal listing for any class of the company's common equity that the company is aware of any material non-compliance with a continued listing standard of the exchange, the company must, within four business days after providing this notice, file with the SEC a current report on Form 8-K disclosing: (a) the date the company provided the notice to the exchange; (b) the continued listing standard that the company fails, or has failed, to meet; and (c) any action that, when the Form 8-K is filed, the company has decided to take concerning its non-compliance. In the release adopting this requirement, the SEC stated that this disclosure is required if a particular exchange rule specifically provides that a particular officer or other authorized individual, such as the CEO, must provide the notice to the exchange, rather than the company itself.

CHAPTER 11.

OFFICER, DIRECTOR AND SHAREHOLDER REPORTING

A. Section 16 Officer, Director and Shareholder Reports

Executive officers, directors, and shareholders of U.S. issuers with equity securities registered under the Exchange Act are subject to the reporting requirements of Section 16(a) of the Exchange Act, the short-swing profit recapture provisions of Section 16(b), and the short sale prohibition of Section 16(c).

1. Section 16 Shareholder Reporting, Profit Recapture and Prohibition on Short Sales

Section 16 of the Exchange Act provides that an officer, director or beneficial owner of greater than 10% of any class of equity securities registered under the Exchange Act (“10% holder”):

- (a) must report initial ownership at the time of registration or upon becoming an officer, director or 10% holder on Form 3;
- (b) must report most changes in beneficial membership of any equity securities of the issuer on Form 4 within two business days of execution of the purchase or sale;
- (c) must file a summary report on Form 5 annually for securities transactions not required to be reported on Form 4 or for any failure to report on a Form 4 during the prior fiscal year, within 45 days of the fiscal year end;
- (d) is liable to forfeit to the issuer any profit made from any purchase and sale or sale and purchase (unless exempt) of equity securities (and related derivative securities) of the issuer within any six month period; and
- (e) is prohibited from making short sales of the issuer’s securities.

Forms 3, 4 and 5 must be filed by insiders with the SEC, and copies must be provided to the issuer and each exchange on which the issuer’s securities are listed (unless the issuer has properly designated one exchange to receive Section 16 filings).

Section 16 is very complex. Errors are easily made through inadvertence or misunderstanding and the consequences of error may be severe.

2. Foreign Private Issuers Exempt. Officers, directors and shareholders of foreign private issuers are exempt from Section 16.

3. Reporting Obligations of Officers and Directors. The reporting obligations apply to officers, directors and 10% shareholders under Section 16(a).

(a) Officers Who Must Report. The following persons are generally deemed to be an “officer” for purposes of Section 16: (i) the president; (ii) the principal financial officer; (iii) the principal accounting officer or, if there is no such accounting officer, the controller; (iv) any vice president in charge of a principal business unit, division or function (such as sales, administration or finance); (v) any other officer of the issuer or its subsidiaries who performs a policy-making function; and (vi) any other person who performs similar policy-making functions for the issuer. Additionally, it is presumed that any person identified by the Company in its public filings as an “executive officer” under Item 401(b) of Regulation S-K is an “officer” under Section 16.

(b) Beneficial Ownership. To ascertain whether a person is the “beneficial owner” of more than 10% of a class of equity securities registered under the Exchange Act, the beneficial ownership standard of Section 13(d) of the Exchange Act is used, except that certain U.S. and non-U.S. institutions are not deemed to be beneficial owners of securities held for the benefit of third parties or in customer or fiduciary accounts. Under Section 13(d), beneficial ownership is deemed to exist if the person has or shares: (i) voting power (including the power to vote or direct the vote) of the security, or (ii) investment power (including the power to dispose or direct the disposition) of the security. Securities issuable under derivative securities that are exercisable or convertible within 60 days are deemed to be beneficially owned for Section 13(d) purposes. For all other purposes under Section 16 (i.e., reporting and liability purposes), a person is deemed the beneficial owner of all securities in which he has or shares a “pecuniary interest.” “Pecuniary interest” means having the opportunity to profit or share in the profit from a transaction in the relevant securities.

(c) “Derivative” and “Non-Derivative” Securities. Filings on Forms 3, 4 and 5 must be made for all derivative and non-derivative securities of an issuer. Generally, “derivative securities” under Section 16 are: any option, warrant, convertible security, stock appreciation right (“SAR”), or similar right with an exercise or conversion privilege at a price related to an equity security, or similar securities with a value derived from the value of an equity security. Generally, “non-derivative securities” are the underlying equity securities (i.e., the common shares). Thus, as grants of options are made under the issuer’s stock plans, a Form 4 must be filed for officers and directors receiving option grants.

The rules presume that ownership of derivative securities is the functional equivalent of owning the underlying securities. Therefore, the acquisition of the derivative securities, rather than exercise, exchange or conversion of derivative securities, is the event that can be “matched” against sales of the underlying securities or other derivative securities. The exercise of the derivative securities merely shifts the form of ownership from indirect to direct and does not give rise to liability for short-swing profits, subject to certain conditions. Consequently, derivative securities are reportable when acquired or granted, rather than when exercised.

(d) What to Report in Filings. The Form 3 must reflect beneficial ownership of all non-derivative securities (e.g., common shares) and all derivative securities (including stock options) of the officer or director at the time of filing. Information must be furnished separately for those securities that are directly owned and for those that are indirectly owned, and separately for each different type of indirect ownership (e.g., common shares owned by the

reporting person's spouse or by a trust, corporation or partnership controlled by the reporting person).

The following changes must be reported on a Form 4:

- (i) all transactions not exempt from Section 16(b) of the Exchange Act (as discussed below);
- (ii) all transactions exempt from Section 16(b) under Rule 16b-3(d), (e), or (f) under the Exchange Act; and
- (iii) all exercises or conversions of a derivative security, whether or not the exercise or conversion is exempt from Section 16(b).

Changes in beneficial ownership must be reported on a Form 4 by the end of the second business day following execution of the transaction. Changes in beneficial ownership include any changes in derivative and non-derivative securities directly or indirectly beneficially owned.

Most transactions between officers and directors and the issuer, or an employee benefit plan of the issuer, must be reported on Form 4. This includes: (i) grants, awards and other acquisitions of securities from the issuer; (ii) dispositions of securities to the issuer; and (iii) certain "discretionary transactions" (defined in Rule 16b-3(b) under the Exchange Act) for which the reporting person can select the date of execution. Additionally, small acquisitions (up to \$10,000 in market value) from the issuer or an employee benefit plan of the issuer must also be reported on Form 4. The subsequent exercise or conversion of a derivative security, although not deemed a "purchase" for Section 16(b) purposes (and thus exempt from Section 16(b) liability), must be reported on a Form 4.

A Form 5 filing must be made to report: (i) transactions during the issuer's most recent fiscal year that were exempt from potential Section 16(b) liability (i.e., gifts and inheritances), except for: (1) transactions exempt from Section 16(b) under Rule 16b-3(d), (e), or (f) (which must be reported on Form 4); (2) exercises and conversions of derivative securities exempt under either Rule 16b-3 or Rule 16b-6(b) under the Exchange Act (which must be reported on a Form 4 on a current basis); (3) transactions exempt from Section 16(b) under Rule 16b-3(c), which are exempt from Section 16(a) of the Exchange Act; and (4) transactions exempt from Section 16 of the Exchange Act under another Section 16(a) rule; (ii) acquisitions, other than from the issuer or an employee benefit plan of the issuer, of less than \$10,000 in market value within a six-month period ("small acquisitions"); and (iii) all holdings and transactions that should have been, but were not, reported on a Form 3 or Form 4 during the most recent fiscal year.

A Form 5 must be filed within 45 days after the end of the company's fiscal year. Many issuers require officers and directors to represent in their annual directors' and officers' questionnaire or in a separate letter delivered after year end that either: (i) they have timely reported all transactions during the prior fiscal year and, accordingly, are not required to make a Form 5 filing; or (ii) they have filed a required Form 5 in a timely manner.

(e) What Transactions are Not Reported. The following transactions need not be reported on either a Form 4 or a Form 5:

- (i) stock splits, stock dividends, “spin-offs” or other dividend transactions in which equity securities of a different issuer are distributed to insiders of the issuer;
- (ii) acquisitions under a dividend or interest reinvestment plan if the plan provides for broad-based participation, does not discriminate in favor of employees of the issuer, and operates on substantially the same terms for all plan participants;
- (iii) acquisitions of rights, such as shareholder or pre-emptive rights, under a pro rata grant to all holders of the same class of equity securities registered under the Exchange Act;
- (iv) certain transactions within “tax-conditioned plans,” except for “discretionary transactions”;
- (v) acquisitions or dispositions of the issuer’s securities under a domestic relations order meeting certain conditions of the Internal Revenue Code;
- (vi) transactions effecting a mere change in the form of beneficial ownership without changing a person’s pecuniary interest in the subject equity securities, other than the exercise or conversion of a derivative security or deposit into or withdrawal from a voting trust; and
- (vii) cancellations or expirations of long derivative security positions where no value is received from the cancellation or expiration.

Additionally, any officer or director who ceases to be an officer or director is only required to continue to report transactions that: (i) are not exempt from the Section 16(b) short-swing profit recovery rules, and (ii) occur within six months of an “opposite-way” transaction executed before the date of ceasing to be an officer or director. For example, if an officer purchases common shares on October 15th and resigns from the issuer on December 31st, any sales of common shares by the officer during the period from January 1st through April 15th (the six month anniversary of the last transaction that occurred while the person was an officer of the issuer) are reportable on Form 4 and may be subject to short-swing liability.

(f) Recapture of Short-Swing Profits.

The combination of the reporting requirements discussed above and the recapture of “short-swing” profits is intended to prevent unfair trading on inside information. Under Section 16(b) of the Exchange Act, any profits (including paper profits) made by a Section 16 reporting person as a result of any combination of purchases and sales (or sales and purchases) of the equity securities in any six-month period belong to and are recoverable by the

issuer. It does not matter whether or not the same securities are involved in both the purchase and sale (or the sale and purchase), and losses cannot be offset against gains. The lowest purchase price is matched with the highest sale price within any six-month period, and any profits are considered the property of the issuer. Good faith on the part of the insider is not a defense, and if the issuer does not claim the profit, any shareholder may press a claim by suing the insider on behalf of the issuer.

In calculating the amount of short-swing profit recoverable for the purchase or sale of derivative securities, derivative securities and the underlying securities are treated alike. Consequently, transactions in derivative securities can be matched with transactions in other securities or in the underlying securities. The maximum amount recoverable by the issuer is the difference in market price of the underlying security on the date of purchase and date of sale.

Certain transactions are exempt from the Section 16(b) short-swing profit recapture rule. These transactions are not “matched” with “opposite-way” transactions (e.g., a purchase with a sale) to determine potential liability under Section 16(b). Examples of transactions exempt from Section 16(b) liability include: (i) transactions (other than discretionary transactions) made by an officer or director under a tax-conditioned employee benefit plan; (ii) specific acquisitions or dispositions approved in advance by either: (1) the board of directors or a committee of the board composed solely of two or more non-employee directors, or (2) the shareholders; and (iii) dispositions directly to the issuer (e.g., the surrender to the issuer of a stock option as part of its exercise in accordance with its terms and the exercise of an option by delivery of owned common shares or the withholding of common shares otherwise issuable upon that exercise).

Because of the mechanical way in which the short-swing trading rules are applied, inadvertent violations easily occur. Therefore, trading by officers and directors should be done carefully.

(g) Prohibition on Short Sales.

Section 16(c) of the Exchange Act prohibits all officers and directors from selling short any equity security of the issuer (other than an exempted security). This provision is intended to prevent officers and directors from profiting by a decline in the price of the issuer’s securities.

B. Schedules 13D and 13G: Beneficial Ownership Reports

The “Williams Act” provisions of the Exchange Act were intended, in part, to provide notice to the public of certain large accumulations of shares and to regulate the conduct of tender offers. Beneficial owners of more than 5% of a voting class of equity securities registered under the Exchange Act (including securities of foreign private issuers) must comply with the beneficial ownership reporting requirements of Section 13(d) of the Exchange Act and Schedules 13D and 13G. Generally, once a voting class of an issuer’s securities is registered under the Exchange Act, any person (or group of persons) who acquires more than 5% of the class must file with the SEC (and deliver to the issuer and each national securities exchange where the

security is traded) a “long form” Schedule 13D disclosure statement within 10 days following the acquisition (i.e., within 10 days after crossing the 5% limit). Schedule 13D elicits certain information as to the identity of the beneficial owner, the pattern of his recent purchases, the source of funds for his purchases, his aggregate holdings and his intentions concerning the company. The schedule is often filed in connection with a tender offer.

Amendments to Schedule 13D must be filed “promptly” (generally within two to three days, but sometimes sooner) to disclose material changes in the percentage of the subject class beneficially owned. An acquisition or disposition of 1% or more of the subject class of securities is deemed to be a material change, and lesser acquisitions or dispositions may be material depending on the facts and circumstances. No filing is required where a change in the percentage of shares owned by a reporting person is caused solely by a change in the number of outstanding shares.

Under Section 13(d), “beneficial ownership” is broadly defined, and is generally found to exist whenever a person has or shares the right to, directly or indirectly, vote or dispose (or direct the voting or direct the disposition) of equity securities. Consequently, shares may be beneficially owned by more than one person. A person will be deemed to be the beneficial owner of a security if that person has the right to acquire beneficial ownership of the security within 60 days including, but not limited to, any right to acquire: (a) through the exercise of any option, warrant or right; (b) through the conversion of a security; (c) under the power to revoke a trust, discretionary account or similar arrangement; or (d) under the automatic termination of a trust, discretionary account or similar arrangement.

There are three exemptions from the obligation to file a Schedule 13D. Where an exemption is available, the acquiring person is required, or, in certain circumstances, permitted to file a “short form” disclosure statement on Schedule 13G. Persons exempt from filing a “long form” Schedule 13D include:

- (a) any person who is the beneficial owner of more than 5% of a registered class of an issuer’s equity securities before and after the effective date of the issuer’s Exchange Act registration statement, and who does not thereafter acquire more than 2% of the outstanding securities during any 12 month period;

- (b) investors owning less than 20% of an outstanding class of registered equity securities and that have not acquired and who do not hold the securities with the purpose or effect of changing or influencing the control of the issuer (“passive investors”); and

- (c) certain “qualified institutional investors” who acquire and hold the securities in the ordinary course of business and not with the purpose or effect of changing or influencing the control of the issuer. These institutions include, e.g.: (i) securities broker-dealers, investment advisers and investment companies registered with the SEC; (ii) banks and insurance companies regulated in the United States; (iii) employee benefit plans and pension plans subject to ERISA; and (iv) related holding companies. (See Rule 13d-1(b)(1)(ii)(A) through (I) under the Exchange Act, listing the U.S. institutions that are “qualified institutional investors.”)

Non-U.S. institutions that are substantially comparable to the U.S. institutions that are

“qualified institutional investors” also may file a Schedule 13G instead of Schedule 13D. The availability of the exemption enabling non-U.S. institutions to file a short form Schedule 13G is subject to three requirements. First, the non-U.S. institution must certify on Schedule 13G that it is subject to a regulatory scheme substantially comparable to the regulatory scheme applicable to its U.S. counterpart. When making this determination, the non-U.S. institution must consider a number of factors, including whether the institution is engaged in a business similar to the business engaged in by a qualified institutional investor listed in Rule 13d-1(b)(1)(ii)(A) through (I), and whether the non U.S. institution provides protections similar to those offered by its U.S. counterpart (e.g., minimum capital requirements, deposit guarantees, licensing requirements, periodic reporting of information in the home country, power of inspection by home country regulators, etc.). Second, in its certification on Schedule 13G, the non-U.S. institution must undertake to provide the SEC staff, upon request, with the information it would otherwise be required to provide in a Schedule 13D. Third, in its certification, the non-U.S. institution must confirm that it acquired and holds the relevant securities in the ordinary course of business and not with the purpose or effect of changing or influencing the control of the issuer.

Passive investors choosing to report ownership on Schedule 13G must initially file that schedule within 10 calendar days after acquiring beneficial ownership of more than 5% of an outstanding class of the issuer’s registered equity securities. All other Schedule 13G filers must file their initial Schedule 13G within 45 days after the end of the calendar year in which they acquired greater than 5% beneficial ownership, except that if a qualified institutional investor acquires more than 10% of the subject class before year-end, it must file the Schedule within 10 days after the end of the first month in which its beneficial ownership exceeded 10%. Generally, amendments reflecting any change in the information reported in Schedule 13G must be filed within 45 days after the end of the year in which the change occurs.

An agreement between two or more persons relating to the acquisition, holding, voting or disposition of the issuer’s equity securities may also result in the creation of a “group” for Section 13(d) reporting purposes. The SEC has intentionally left vague the outer boundaries of the definition of the term “group,” but it is clear that a group may be formed without any formal agreement, oral or written, and may be inferred from circumstantial evidence (e.g., parallel purchases).

CHAPTER 12.

ACCOUNTING

A. Introduction

Financial information may be the most important part of the disclosure public companies provide to shareholders and the capital markets. Audits and financial reporting by public companies are central to the capital formation process and maintaining the integrity of our capital markets. This chapter describes the basic financial statement requirements for companies going public in the United States and reporting thereafter to their shareholders and the markets generally.

B. Financial Reporting

1. Regulation S-X: The Basic Rules for U.S. Issuers

Regulation S-X is the basic accounting regulation of the SEC. Regulation S-X, together with certain financial reporting releases, prescribes the basic form, content and requirements for financial statements required of nearly all issuers for registration statements under the Securities Act, and registration statements, reports, and proxy and information statements under the Exchange Act.

2. Article 8 of Regulation S-X: Scaled Disclosure Requirements for Smaller Reporting Companies

A company that qualifies as a “smaller reporting company” (including a foreign private issuer that uses U.S. issuer forms and prepares its financial statements under U.S. GAAP) may take advantage of certain scaled financial statement requirements contained in Article 8 of Regulation S-X. Smaller reporting companies electing to prepare their financial statements with the form and content required in Article 8 of Regulation S-X need not apply the other form and content requirements in Regulation S-X except that: (a) the report and qualifications of the independent auditor must comply with the requirements of Article 2 of Regulation S-X (as noted below); (b) the description of accounting policies must comply with Article 4-08(n) of Regulation S-X; and (c) smaller reporting companies engaged in oil and gas producing activities must follow the financial accounting and reporting standards specified in Article 4-10 of Regulation S-X for those activities. With regard to pro forma financial information, smaller reporting companies should comply with the requirements of Rule 8-05 of Regulation S-X, but may wish to consider the guidance in Article 11. In other words, to the extent that Article 11-01 of Regulation S-X (Pro Forma Presentation Requirements) offers enhanced guidelines for preparing, presenting and disclosing pro forma financial information, smaller reporting companies may wish to consider these items.

The principal differences between Article 8 and the other Regulation S-X Articles applicable to non-smaller reporting companies are that Article 8 does not have a requirement to file supplemental schedules, does not designate specific financial statement format, does not stipulate quantitative thresholds for many disclosures, and does not have a requirement to file separate financial statements of investees as would be required under Rule 3-09 of Regulation S-

X.

3. Foreign Private Issuers

Item 8.A of Form 20-F specifies the financial statement requirements for a foreign private issuer, the periods to be covered by those financial statements, and the permitted age of the financial statements. Form 20-F is the primary Exchange Act registration statement and annual report form for foreign private issuers. The registration statement forms under the Securities Act for foreign private issuers require them to provide information required by Item 8.A of Form 20-F.

C. Basic Financial Statement Requirements

1. Consolidated Balance Sheets for Filings on Form S-1 (and Certain Other Filings)

Rule 3-01 of Regulation S-X sets out the following requirements:

(a) The issuer must file consolidated audited balance sheets as of the end of each of the two most recent fiscal years. If the issuer has been in existence for less than one fiscal year, the issuer must file an audited balance sheet as of a date within 135 days of the date of filing the registration statement.

(b) If the filing, other than a filing on Form 10-K or Form 10, is made within 45 days after the end of the issuer's fiscal year and audited financial statements for the most recent fiscal year are not available, the balance sheets may be as of the end of the two preceding fiscal years and the filing must include an additional balance sheet as of an interim date at least as current as the end of the issuer's third fiscal quarter of the most recently completed fiscal year.

(c) The instruction in (b) above also applies to filings, other than on Form 10-K or Form 10, made after 45 days but within the number of days of the end of the issuer's fiscal year specified in (i) below, if the following conditions are met: (1) the issuer files annual, quarterly and other reports under Section 13 or 15(d) of the Exchange Act and all reports due have been filed; (2) for the most recent fiscal year for which audited financial statements are not yet available the issuer reasonably and in good faith expects to report income attributable to the issuer, after taxes but before extraordinary items and cumulative effect of a change in accounting principle; and (3) for at least one of the two fiscal years immediately preceding the most recent fiscal year the issuer reported income attributable to the issuer, after taxes but before extraordinary items and cumulative effect of a change in accounting principle.

(d) For filings made after 45 days but within the number of days of the end of the issuer's fiscal year specified in (i) below where the conditions in (c) above are not met, the filing must include the audited balance sheets required by (a) above.

(e) For filings made after the number of days specified in (i) below, the filing must also include a balance sheet as of an interim date within the following number of days of the date of filing: (1) 130 days for large accelerated filers and accelerated filers, and (2) 135 days for all other issuers.

(f) Any interim balance sheet provided in accordance with the requirements of Rule 3-01 of Regulation S-X may be unaudited and need not be presented in greater detail than is required by Rule 10-01 of Regulation S-X. Notwithstanding the requirements of Rule 3-01, the most recent interim balance sheet included in a filing must be at least as current as the most recent balance sheet filed with the SEC on Form 10-Q.

(g) For filings by registered management investment companies, the requirements of Rule 3-18 of Regulation S-X apply in lieu of the requirements of Rule 3-01.

(h) Any foreign private issuer, other than a registered management investment company or an employee plan, may file the financial statements required by Item 8.A of Form 20-F in lieu of the financial statements specified in Rule 3-01.

(i) For (c) and (d) above, the number of days is: (1) 60 days for large accelerated filers, (2) 75 days for accelerated filers, and (3) 90 days for all other issuers. For (e) above, the number of days is: (1) 129 days after the end of the issuer's most recent fiscal year for large accelerated filers and accelerated filers, and (2) 134 days after the end of the issuer's most recent fiscal year for all other issuers.

The following explains some of requirements discussed above:

(A) General Rule: The latest balance sheet must be as of a date no more than 134 days for non-accelerated filers (or 129 days for accelerated and large accelerated filers, or 180 days on Form 1-A) before the effective date of the registration statement (or date the proxy statement is mailed). Example: A Form S-1 of a non-accelerated filer with an audited June 30th balance sheet (June year-end) cannot be declared effective after November 11th without updating.

(B) Rule for Initial Filers: The balance sheet date in an initial registration statement should not be more than 134 days old, except that third quarter data is timely through the 45th day after the most recent fiscal year-end. After the 45th day, audited financial statements for that fiscal year must be included in the registration statement. The financial information in an initial registration statement for a smaller reporting company may be up to 90 days after year-end if the issuer expects to report income in the current year and has reported income in at least one of the two previous years. Example: A Form S-1 for an issuer with a calendar year-end with an interim balance sheet as of the end of the first quarter (March 31) cannot be declared effective after August 12th without updating to the end of the second quarter (June 30). A Form S-1 for a calendar year-end company other than a smaller reporting company with an interim balance sheet as of September 30 cannot be declared effective after February 14th.

(C) Year-End Rule for Reporting Companies: Reporting companies required to file under Section 13(a) or 15(d) of the Exchange Act do not need to update third quarter interim financial statements until the 90th day for non-accelerated filers (or the 75th day for accelerated filers, and the 60th day for large accelerated filers) after their fiscal year-end, if they meet the three conditions of Rule 3-01(c) (Rule 8-08(b) for smaller reporting companies): (1) they have filed all Exchange Act reports due, (2) they expect to report income in the year just completed, and (3) they reported income in at least one of the two previous years. Unless all

three conditions are met, if the SEC staff accelerates the effective date of the registration statement after the 45th day following the fiscal year-end, it will request the company to include audited financial statements for the most recently completed fiscal year. This 45-day rule applies to both smaller reporting companies and non-smaller reporting companies. Regarding condition (1) above: A reporting company that has not filed its first Exchange Act report since an initial offering has not met condition (1). Regarding conditions (2) and (3) above: For smaller reporting companies, these conditions are based on income from continuing operations before taxes. It correlates to line item 14 in Rule 5-03(b) of Regulation S-X after adding back tax expense per line 11. For other reporting companies, these conditions are based on income after taxes, but before extraordinary items and cumulative effect of a change in accounting principle. It is income after reported discontinued operations, and correlates to line item 16 in Rule 5-03(b) of Regulation S-X. If audited financial statements for the most recently completed fiscal year are available or become available before the effective date of the registration statement or the mailing date of a proxy statement, they must be included in the filing. Availability is determined on a facts and circumstances basis. Financial statements become available no later than when they are “issued” based on the staff guidance in Topic D-86, contained in Appendix D to the EITF Abstracts.

(D) Newly Formed Issuer That Does Not Have Predecessor Operations: For an issuer that was not in existence at the end of its most recently completed fiscal year, audited financial statements are required as of a date less than 135 days before the initial filing date of the registration statement. Subsequent updates to comply with the 135 day rule may be made on an unaudited basis, except that audited financial statements are required if the effective date of the registration statement is more than 45 days after the company’s fiscal year end.

2. Consolidated Statements of Income, Cash Flows and Stockholders’ Equity

For filing a Form S-1, the issuer must include consolidated audited statements of income, cash flows and stockholders’ equity for each of the three fiscal years preceding the date of the most recent audited balance sheet being filed, or such shorter period as the issuer (including any predecessors) has been in existence. Additionally, the issuer must include interim statements of income, cash flows and stockholders’ equity for any interim period between the latest audited balance sheet and the date of the most recent interim balance sheet being filed in the registration statement, and a comparable statement of income and cash flows for the corresponding period of the preceding fiscal year. Such interim financial statements may be unaudited and need not be presented in greater detail than is required by Rule 10-01 of Regulation S-X. (See Rule 3-02 of Regulation S-X, which concerns consolidated statements of income and changes in financial positions, and Rule 3-04 of Regulation S-X, which concerns changes in stockholders’ equity and noncontrolling interests.)

For filings by registered management investment companies, the requirements of Rule 3-18 of Regulation S-X apply in lieu of the requirements of Rule 3-02.

Any foreign private issuer, other than a registered management investment company or an employee plan, may file the financial statements required by Item 8.A of Form 20-F in lieu of the financial statements specified in Rule 3-02.

3. Financial Statements of Businesses Acquired or to be Acquired

Oftentimes, a company's initial public offering is centered around a recent acquisition or series of acquisitions or an acquisition to be consummated contemporaneously with or shortly after consummation of the public offering. In that case, issuers must pay special attention to the specific provisions of Rule 3-05 of Regulation S-X for financial statements of businesses acquired or to be acquired where the issuer must use Form S-1 for its registration statement. However, for smaller reporting companies filing registration statements, the SEC has relaxed the reporting requirements for acquired businesses that are to be reflected in registration statements. (See Rule 8-04 of Regulation S-X.)

4. Article 8 of Regulation S-X – Financial Statement Requirements for Smaller Reporting Companies

(a) Relaxed Requirements. Article 8 of Regulation S-X relaxes the financial statement requirements for smaller reporting companies.

(b) Annual Financial Statements. Smaller reporting companies are required to file an audited balance sheet as of the end of each of the most recent two fiscal years, or as of a date within 135 days of the filing date if the issuer has existed for a period of less than one fiscal year. Additionally, the issuer must furnish audited statements of income, cash flows and changes in stockholders' equity for each of the two fiscal years preceding the date of the most recent audited balance sheet (or such shorter period as the issuer has been in business).

(c) Interim Financial Statements. Interim financial statements may be unaudited; however, before filing, interim financial statements included in quarterly reports on Form 10-Q must be reviewed by an independent public accountant using professional standards and procedures for conducting such reviews, as established by generally accepted auditing standards, as may be modified or supplemented by the SEC. If, in any filing, the issuer states that interim financial statements have been reviewed by an independent public accountant, a report of the accountant on the review must be filed with the interim financial statements. Interim financial statements must include a balance sheet as of the end of the issuer's most recent fiscal quarter, a balance sheet as of the end of the preceding fiscal year, and income statements and statements of cash flows for the interim period up to the date of such balance sheet and the comparable period of the preceding fiscal year. Article 8 also contains relaxed provisions for the condensed format for interim financial statements, disclosure requirements as to content of footnotes, information concerning material subsequent events and contingencies and certain other items.

5. Form 20-F – Financial Statement Requirements for Foreign Private Issuers

Form 20-F (either as a registration statement or annual report) must contain audited consolidated statements of income and cash flow for the issuer's three most recently completed fiscal years and balance sheets as of the end of the three most recently completed fiscal years. However, a foreign issuer need not provide a balance sheet for the earliest of the three years if that balance sheet is not required by a jurisdiction outside the United States. Unaudited six-month financial statements must be included in Form 20-F registration statements

(but not annual reports) if the registration statement is filed more than nine months after the end of the last fiscal year for which audited statements are provided. (See the discussion below.)

Financial statements included in a Form 20-F registration statement or annual report may be prepared under U.S. GAAP, IFRS or GAAP of an appropriate foreign country. If prepared other than under U.S. GAAP or IASB IFRS, the annual and interim financial statements included in the filing must be reconciled to U.S. GAAP under: (a) either Item 17 or Item 18 of Form 20-F for fiscal years ending before December 15, 2011; and (b) Item 18 of Form 20-F for fiscal years ending on or after December 15, 2011. The reconciliation of the income statement of the earliest of the three fiscal years presented may be omitted if the information has not previously been included in an SEC filing. This normally occurs when Form 20-F is used as an Exchange Act registration statement.

Reconciliation to U.S. GAAP under Item 17 of Form 20-F requires the inclusion of a financial statement footnote disclosing the material differences between U.S. GAAP and the accounting principles employed in preparing the financial statements, and reconciling the entries in the financial statements to reflect the differences that would result if U.S. GAAP had been employed.

Reconciliation to U.S. GAAP under Item 18 of Form 20-F requires the preparation of the financial statement footnotes required under U.S. GAAP for a U.S. issuer.

Regarding registration and reporting under the Exchange Act, for fiscal years ending before December 15, 2011, the issuer may choose whether to comply with Item 17 or Item 18 in preparing its U.S. GAAP reconciliation. Item 18 is significantly more burdensome than Item 17. Nevertheless, many issuers comply with Item 18 because, for fiscal years ending before December 15, 2011, Item 18 reconciliation is required in most Securities Act registration statements for public securities offerings in the United States, and these issuers do not wish to be delayed by the preparation of an Item 18 reconciliation if they later decide to do a U.S. public offering.

To (a) ensure that the same type of financial information is provided regardless of the type of public securities offering that is being made, and (b) eliminate the distinction between the disclosure provided to the primary and secondary markets, the SEC amended Form 20-F and the registration statement forms available to foreign private issuers under the Securities Act (Forms F-1, F-3, and F-4) to require the disclosure of financial information according to Item 18 of Form 20-F for registration statements filed under both the Exchange Act and the Securities Act, as well as for Exchange Act annual reports. Foreign private issuers will be required to comply with these amendments beginning with their first fiscal year ending on or after December 15, 2011. Accordingly, a foreign private issuer that currently prepares its financial statements according to Item 17 of Form 20-F will not be required to prepare financial statements under Item 18 until it files an annual report for its first fiscal year ending on or after December 15, 2011. The SEC did not eliminate the availability of Item 17 disclosures for Canadian issuers filing under the MJDS. Item 17 also will continue to be available for financial statements of non-registrants that are required to be included in a foreign or U.S. issuer's registration statement, Exchange Act annual report, or other Exchange Act report. These include, e.g.: (a) significant acquired businesses under Rule 3-05 of Regulation S-X, (b) significant equity method

investees under Rule 3-09 of Regulation S-X, and (c) exempt guarantors under Rule 3-10(i) of Regulation S-X. Item 17 will also continue to be permitted for pro forma information under Article 11 of Regulation S-X.

Regarding the age of financial statements in a registration statement (Item 8 of Form 20-F):

Financial statements of a foreign private issuer must be as of a date within nine months of the effective date of a registration statement. Audited financial statements for the most recently completed fiscal year must be included in registration statements declared effective three months or more after fiscal year-end. Under the rule, a registration statement of a foreign private issuer may become effective with audited financial statements as old as 15 months, with the most recent interim statements as old as nine months. If interim statements are required, they must cover a period of at least six months.

The 15 month period for audited statements is extended to 18 months, and the nine month period for interim statements is extended to 12 months, for offerings of securities: (a) upon the exercise of outstanding rights granted pro rata to all existing security holders; (b) under a dividend or interest reinvestment plan; or (c) upon the conversion of outstanding convertible securities or upon the exercise of outstanding transferable warrants issued by the issuer or by an affiliate of the issuer.

There is a special rule for foreign private issuer IPOs. Audited financial statements in initial public offerings must be no more than 12 months old at the time of filing. However, this rule applies only where the issuer is not public in any jurisdiction. The issuer may request a waiver from the SEC staff of the 12-month requirement where compliance is not required in any other jurisdiction and compliance is impracticable or involves undue hardship.

The age requirements in Item 8 of Form 20-F also apply to financial statements of: (a) foreign businesses acquired by both foreign and U.S. issuers under Rule 3-05 of Regulation S-X, including filings by U.S. issuers under Items 2.01 and 9.01 of Form 8-K; (b) foreign target businesses required in Form S-4 or Form F-4; (c) foreign equity investees of both foreign and U.S. issuers under Rule 3-09 of Regulation S-X; (d) foreign businesses that are acquired real estate operations under Rule 3-14 of Regulation S-X; and (e) financial statements of affiliates whose securities collateralize a security being registered as required by Rule 3-16 of Regulation S-X.

A foreign private issuer that has been in existence less than a year must include an audited balance sheet that is no more than nine months old. If the foreign private issuer has commenced operations, audited statements of income, stockholders' equity and cash flows for the period from the date of inception to the date of the audited balance sheet also are required.

If financial information reporting revenues and income for an annual or interim period more current than otherwise required by Item 8 of Form 20-F is made available to shareholders, exchanges, or others in any jurisdiction, that information should be included in the registration statement. (See Item 8.A.5 of Form 20-F.) The more current information is not required to be reconciled to U.S. GAAP. However, a narrative explanation of differences in

accounting principles should be provided, and material new reconciling items should be quantified. Differences between foreign and U.S. GAAP can be identified by cross-reference to U.S. GAAP reconciliation footnotes elsewhere in the filing. (Note that the reconciliation requirements do not apply to issuers filing audited financial statements prepared under IFRS as issued by the IASB.)

Occasionally, the interim information that is publicly distributed in the issuer's home country will be prepared using accounting standards that are different from those used in the U.S. registration statement. For example, a foreign issuer may use U.S. GAAP in its primary financial statements in filings with the SEC, but reports in a foreign GAAP in its home country. The company releases more recent earnings information in its home country in foreign GAAP. Item 8.A.5 requires that information to be included in the prospectus. In this instance, the U.S. investor has not had the benefit of knowing the reconciling items between home country GAAP and U.S. GAAP. Therefore, the information disclosed under Item 8.A.5 would need to be supplemented with a description and quantification of differences in accounting principles. In this situation, an issuer may either: (a) reconcile the Item 8.A.5 information to U.S. GAAP, or (b) provide a reconciliation from U.S. GAAP to foreign GAAP (reverse reconciliation) for at least the most recent fiscal year required in the registration statement.

Inclusion of published information under Item 8.A.5 does not ordinarily trigger a requirement to include full interim financial statements more recent than otherwise required. For example, if complete financial statements related to the most recent quarter (but not the comparative period) are distributed in a foreign issuer's home country, that information must be included in the U.S. registration statement. Comparative prior period information is not required because the information provided is included only because of Item 8.A.5. To avoid confusing U.S. readers, the issuer should include disclosure explaining why the information is provided particularly when the information is placed with other financial statements and may look incomplete.

However, if the information provided contains a reconciliation to U.S. GAAP, the SEC staff believes that inclusion of reconciled information for the comparative prior periods generally will also be necessary to prevent the current period information from being misleading. A foreign private issuer is not ordinarily required to provide U.S. GAAP information in its home jurisdiction. Accordingly, when a foreign private issuer presents more current U.S. GAAP information, it effectively has decided to present interim financial statements, and is also required to present comparatives as required by Item 8.A.5 of Form 20-F. In these circumstances, the current and comparative interim period would need to be covered by MD&A (discussed below) and pro forma information would need to be updated to that date.

D. MD&A Disclosure

In addition to the financial statements, companies must also address and explain accounting matters in the part of the prospectus called "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A"), as well as the MD&A section of subsequent periodic reports they file with the SEC after becoming a publicly held company.

1. The Purpose of MD&A Disclosure. Disclosure in the MD&A is intended to increase the transparency of an issuer's financial condition and performance. The MD&A is also intended for management to: (a) provide investors with an understanding of management's view of the financial performance and condition of the company, (b) describe what the financial statements do not show, and (c) describe important trends that have shaped the past or are reasonably likely to shape the future.

2. Basic MD&A Items for Disclosure. The MD&A rules are intended to elicit disclosure of:

(a) information necessary to an understanding of the issuer's financial condition, changes in financial condition and results of operations;

(b) any known trends, demands, commitments, events or uncertainties that will result in, or that are reasonably likely to result in, the issuer's liquidity increasing or decreasing in any material way and, if a material deficiency is identified, the course of action that the issuer has taken or proposes to take to remedy the deficiency;

(c) the issuer's internal and external sources of liquidity, and any material unused sources of liquid assets;

(d) the issuer's material commitments for capital expenditures as of the end of the latest fiscal period, the general purpose of such commitments, and the anticipated source of funds needed to fulfill such commitments;

(e) any known material trends, favorable or unfavorable, in the issuer's capital resources, including any expected material changes in the mix and relative cost of such resources, considering changes between equity, debt and any off-balance sheet financing arrangements;

(f) any unusual or infrequent events or transactions or any significant economic changes that materially affected the amount of reported income from continuing operations and, in each case, the extent to which income was so affected;

(g) any other significant components of revenues or expenses that, in the issuer's judgment, should be described in order to understand the issuer's results of operations;

(h) any known trends or uncertainties that have had, or that the issuer reasonably expects will have, a material favorable or unfavorable impact on net sales or revenues or income from continuing operations and, if the issuer knows of events that will cause a material change in the relationship between costs and revenues (such as known future increases in costs of labor or materials or price increases or inventory adjustments), the change in the relationship;

(i) the extent to which material increases in net sales or revenues are attributable to increases in prices or to increases in the volume or amount of goods or services being sold or to the introduction of new products or services;

(j) the impact of inflation and changing prices on the issuer's net sales and revenues and on income from continuing operations for the three most recent fiscal years of the issuer or for those fiscal years in which the issuer has been engaged in business, whichever period is shortest;

(k) in a separately-captioned section, the issuer's off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the issuer's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors, including the following four items to the extent necessary to an understanding of such arrangements and effect (and such other information that the issuer believes is necessary for such an understanding): (1) the nature and business purpose to the issuer of such off-balance sheet arrangements; (2) the importance to the issuer of such off-balance sheet arrangements in respect of its liquidity, capital resources, market risk support, credit risk support or other benefits; (3) the amounts of revenues, expenses and cash flows of the issuer arising from such arrangements; the nature and amounts of any interests retained, securities issued and other indebtedness incurred by the issuer in connection with such arrangements; and the nature and amounts of any other obligations or liabilities (including contingent obligations or liabilities) of the issuer arising from such arrangements that are or are reasonably likely to become material and the triggering events or circumstances that could cause them to arise; and (4) any known event, demand, commitment, trend or uncertainty that will result in or is reasonably likely to result in the termination, or material reduction in availability to the issuer, of its off-balance sheet arrangements that provide material benefits to it, and the course of action that the issuer has taken or proposes to take in response to any such circumstances;

(l) contractual obligations in a tabular format (see, e.g., Item 303(a)(5) of Regulation S-K);⁹⁷

(m) matters that will have an effect on future operations and have not had an effect in the past; and

(n) matters that have had an effect on reported operations and are not expected to have an effect upon future operations.

E. Non-GAAP Financial Measures

Regulation G requires reporting issuers (other than registered investment companies) that publicly disclose or release financial information that is calculated and presented on the basis of methodologies other than U.S. GAAP (i.e., non-GAAP financial measures) to include, in that disclosure or release, a presentation of the most directly comparable GAAP financial measure and a reconciliation of the disclosed non-GAAP financial measure to the most directly comparable GAAP financial measure.

⁹⁷ All reporting issuers (U.S. issuers and foreign private issuers, except for smaller reporting companies) must disclose in a table in the MD&A section of their annual reports their aggregate amounts of payments due under specified categories of (known) contractual obligations broken down over time. This requirement is intended to enable investors to assess the issuer's short-term and long-term liquidity and capital resources needs.

Under Regulation G, a “non-GAAP financial measure” is a numerical measure of an issuer’s historical or future financial performance, financial position or cash flows that:

- excludes amounts, or is subject to adjustments that have the effect of excluding amounts, that are included in the most directly comparable measure calculated and presented under U.S. GAAP in the statement of income, balance sheet, or statement of cash flows (or equivalent statements) of the issuer; or
- includes amounts, or is subject to adjustments that have the effect of including amounts, that are excluded from the most directly comparable measure so calculated and presented.

However, Regulation G does not apply to public disclosure of a non-GAAP financial measure by or on behalf of a foreign private issuer if the following three conditions are met:

- the issuer’s securities are listed or quoted on a securities market (i.e., an exchange or inter-dealer quotation system) outside the United States;
- the non-GAAP financial measure is not derived from or based on a measure calculated and presented under U.S. GAAP; and
- the disclosure is made by or on behalf of the foreign private issuer outside the United States, or is included in a written communication that is released by or on behalf of the issuer outside the United States.

This limited exemption for foreign private issuers will still apply despite the existence of one or more of the following circumstances:

- a written communication is released in the United States as well as outside the United States, so long as the communication is released in the United States contemporaneously with or after the release outside the United States and is not otherwise targeted at persons located in the United States;
- foreign or U.S. journalists or other third parties have access to the information;
- the information appears on one or more web sites of the issuer, so long as the web sites, taken together, are not available exclusively to, or targeted at, persons located in the United States; or
- after the disclosure or release of the information outside the United States, the information is furnished to the SEC under Form 6-K.

F. Internal Control Over Financial Reporting

Under Rules 13a-15 and 15d-15 under the Exchange Act, reporting issuers must:

- (a) maintain “internal control over financial reporting” (defined below);

(b) through their management, evaluate (with the participation of the CEO and CFO, or persons performing similar functions) the effectiveness of the issuer's internal control over financial reporting as of the end of each fiscal year; and

(c) through their management, evaluate (with the participation of the CEO and CFO, or persons performing similar functions) any change in the issuer's internal control over financial reporting that occurred during each of the issuer's fiscal quarters (or fiscal year for a foreign private issuer) that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting.

"Internal control over financial reporting" is a process designed by, or under the supervision of, the issuer's CEO and CFO, or persons performing similar functions, and effected by the issuer's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP and includes those policies and procedures that: (a) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer; (b) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and (c) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the issuer's assets that could have a material effect on the financial statements.

Each annual report must include a top-down, risk-based evaluation by management of internal control over financial reporting. The assessment should evaluate whether controls have been implemented to adequately address the risk that a material misstatement of the financial statements would not be prevented or detected in a timely manner. Management's evaluation of evidence about the operation of its controls should be based on its assessment of risk.

In each annual report, management must provide a report on the issuer's internal control over financial reporting that contains:

(a) a statement of management's responsibility for establishing and maintaining adequate internal control over financial reporting for the issuer;

(b) a statement identifying the framework used by management to evaluate the effectiveness of the issuer's internal control over financial reporting;

(c) management's assessment of the effectiveness of the issuer's internal control over financial reporting as of the end of the issuer's most recent fiscal year, including a statement as to whether or not the issuer's internal control over financial reporting is effective. This discussion must include disclosure of any material weakness in the issuer's internal control over financial reporting identified by management. Management is not permitted to conclude that the issuer's internal control over financial reporting is effective if there are one or more material weaknesses in the issuer's internal control over financial reporting; and

(d) if the issuer is an accelerated filer or a large accelerated filer, or otherwise includes in its annual report an independent auditor's attestation report on internal control over financial reporting, a statement that the independent auditor that audited the financial statements included in the annual report has issued an attestation report on management's assessment of the issuer's internal control over financial reporting.

If the issuer is an accelerated filer or a large accelerated filer, its annual report must include an independent auditor's attestation report on management's assessment of the issuer's internal control over financial reporting. (Under former SEC rules, a non-accelerated filer would have been required to include an attestation report of its independent auditor on internal control over financial reporting in the filer's annual report filed with the SEC for fiscal years ending on or after June 15, 2010. However, in September 2010, the SEC removed the requirement for a non-accelerated filer to include in its annual report an attestation report of the filer's independent auditor. As discussed in (d) above, the SEC also adopted a conforming change to its rules concerning management's disclosure in the annual report regarding inclusion of an attestation report to provide that the disclosure only applies if an attestation report is included. Last, the SEC made a conforming change to Rule 2-02(f) of Regulation S-X to clarify that an auditor of a non-accelerated filer need not include in its audit report an assessment of the issuer's internal control over financial reporting.)

Each issuer's annual report must disclose any change in the issuer's internal control over financial reporting that occurred during the issuer's fourth fiscal quarter (or fiscal year for a foreign private issuer) that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting.

The requirements concerning (a) management's annual report on internal control over financial reporting, and (b) the attestation report of the independent auditor, do not apply to newly public companies. Specifically, an issuer need not comply with these requirements until it either had been required to file an annual report under Section 13(a) or 15(d) of the Exchange Act for the prior fiscal year or had filed an annual report with the SEC for the prior fiscal year. An issuer that does not comply must include a statement in the first annual report that it files in substantially the following form: "This annual report does not include a report of management's assessment regarding internal control over financial reporting or an attestation report of the company's [independent auditor] due to a transition period established by rules of the Securities and Exchange Commission for newly public companies."

The issuer must maintain evidential matter, including documentation, to provide reasonable support for management's assessment of the effectiveness of the issuer's internal control over financial reporting.

The requirements discussed above augment the officer "civil certification" rules (i.e., Rules 13a-14(a) and 15d-14(a) under the Exchange Act, which were adopted under Section 302 of SOX). For example, under the officer civil certification rules, the specified officers must certify in annual and quarterly reports that they: (a) are responsible for establishing and maintaining internal control over financial reporting for the issuer; (b) have designed the internal control over financial reporting, or had the internal control over financial reporting designed under their supervision, to provide reasonable assurance regarding the reliability of financial

reporting and the preparation of financial statements for external purposes in accordance with GAAP; and (c) have disclosed in the periodic report as to which the certification is attached any change in the issuer's internal control over financial reporting that occurred during the issuer's most recent fiscal quarter (for U.S. issuers) or the period covered by the annual report (for foreign private issuers) that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting. Additionally, the specified officers must certify in annual and quarterly reports that they have disclosed, based on their most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions): (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting that are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and (b) any fraud (even if not material) that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Thus, SEC rules require a reporting issuer to make the following disclosures concerning internal control over financial reporting. First, "material weaknesses" must be disclosed: (a) to the audit committee and independent auditor quarterly (annually for foreign private issuers), and (b) to the public in management's annual report on internal control over financial reporting. Second, "significant deficiencies" must be disclosed to the audit committee and independent auditor quarterly (annually for foreign private issuers), but the rules do not require public disclosure of "significant deficiencies" if they are not also "material weaknesses." Third, any fraud, whether or not material, that involves internal control personnel must be disclosed to the audit committee and independent auditor quarterly (annually for foreign private issuers), but the rules do not specifically require public disclosure of the fraud. Last, "material changes" must be disclosed to the public quarterly (annually for foreign private issuers).

Additionally, Section 906 of SOX amended the U.S. Criminal Code and imposed the "criminal certification" for CEOs and CFOs (or their equivalent) of reporting issuers for certain periodic reports. The Section 906 certification must accompany periodic reports containing financial statements filed by a reporting issuer under the Exchange Act (U.S. and foreign). This includes annual and quarterly reports on Form 10-K, 10-Q, 20-F and 40-F, and any amendments to them if the amendments contain financial statements, but not current reports (i.e., Form 8-K or 6-K), even if they contain financial statements. The Section 906 certification requires the issuer's CEO and CFO to certify that: (a) the report containing the financial statements fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act, and (b) information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the issuer. Unlike the Section 302 certification, the SEC has not mandated the specific language for the Section 906 certification. Instead, the SEC rules (see Rules 13a-14(b) and 15d-14(b) under the Exchange Act) simply require certification in the form required by Section 906 of SOX.

G. Selection of Independent Accountants

1. The Accountant as Independent "Watchdog". The U.S. securities laws require that the financial statements of public companies be audited by a "registered public accounting firm" (see H. below) that is "independent" both in fact and in appearance. Both the SEC and the

courts hold that the independence of accountants for a public issuer is one of the most fundamental requirements of the U.S. capital markets. They view an accountant as a “watchdog” for the public, with an ultimate allegiance to the corporation’s creditors and stockholders, as well as to the investing public. While the SEC has made accommodations for foreign private issuers in the area of accounting principles, the SEC has not made similar accommodations in the area of auditing standards. Therefore, foreign private issuers must adhere to the same standards as U.S. issuers for independent accountants.

2. Independence – Not Defined – Based on All Relevant Circumstances. The SEC’s independence rules are set forth in Rule 2-01 of Regulation S-X. Rule 2-01, governing qualifications of accountants for SEC registration and reporting purposes, does not define “independence.” Generally, all relevant circumstances must be examined in determining the independence of accountants, including evidence as to all relationships between the auditor and the issuer (and its affiliates).

Rule 2-01 is designed to ensure that auditors are qualified and independent of their audit clients both in fact and in appearance. Accordingly, the Rule sets forth restrictions, including but not limited to, on financial, employment and business relationships between an accountant and an audit client and restrictions on an accountant providing certain non-audit services to an audit client. These restrictions are set forth in Rule 2-01(c)(1) to (c)(8). The general standard of auditor independence is set forth in Rule 2-01(b). (The general standard is as follows: “The [SEC] will not recognize an accountant as independent, with respect to an audit client, if the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant’s engagement. In determining whether an accountant is independent, the [SEC] will consider all relevant circumstances, including all relationships between the accountant and the audit client, and not just those relating to reports filed with the [SEC].”) Rule 2-01(c) reflects the application of the general standard to particular circumstances. However, Rule 2-01(c) does not purport to, and the SEC could not, consider all circumstances that raise independence concerns, and these are subject to the general standard in Rule 2-01(b). In considering this standard, the SEC looks in the first instance to whether a relationship or the provision of a service: (a) creates a mutual or conflicting interest between the accountant and the audit client; (b) places the accountant in the position of auditing his own work; (c) results in the accountant acting as management or an employee of the audit client; or (d) places the accountant in a position of being an advocate for the audit client. These factors are general guidance only and their application may depend on particular facts and circumstances. Accordingly, issuers and accountants are encouraged to consult with the SEC’s Office of the Chief Accountant before entering into relationships, including relationships involving the provision of services, that are not explicitly described in the Rule. (SEC independence rules also apply to Regulation A and Regulation D filings.)

Auditor reports on financial statements that refer to standards of the Public Company Accounting Oversight Board (“PCAOB”) (see H. below) must comply with the independence rules of both the SEC and the PCAOB. The PCAOB has issued certain independence and ethics rules, which are part of its adopted standards. Compliance with these rules is required to issue a PCAOB opinion.

H. Auditor Registration with the Public Company Accounting Oversight Board (“PCAOB”)

Section 102(a) of SOX requires public accounting firms to register with the PCAOB before preparing or issuing, or participating in the preparation or issuance of, an audit report for any “issuer” (as defined below). To enable public accounting firms to comply with this registration requirement, the PCAOB has adopted rules establishing a registration system.

PCAOB Rule 2100 requires each public accounting firm (U.S. or foreign) that: (a) prepares or issues an audit report for any issuer, or (b) plays a substantial role in the preparation or furnishing of an audit report for any issuer, to be registered with the PCAOB (i.e., to be a “registered public accounting firm”). “Issuer” is defined in PCAOB Rule 1001(i)(iii) to include any U.S. or foreign issuer (as defined in Section 3 of the Exchange Act) that: (a) is reporting under the Exchange Act; or (b) has a Securities Act registration statement pending (i.e., is engaging in an initial public offering in the United States). Section 2(a)(7) of SOX has the same definition.

A public accounting firm not registered with the PCAOB may be able to perform some audit services for an issuer if the firm does not “play a substantial role in the preparation or furnishing of an audit report” as that phrase is defined in PCAOB Rule 1001(p)(ii).

In accordance with PCAOB Rule 2107(b)(1), a firm that was once registered and then later withdrew may reissue or give consent to the use of a prior report that it issued while registered. However, the firm cannot update or dual-date a previously issued report after the firm is no longer registered, as that involves additional audit work.

Issuer financial statements audited by a non-registered firm are considered to be “not audited,” and any Form 10-K, proxy statement or registration statement containing or incorporating by reference such financial statements is deemed substantially deficient. Additionally, the Form 10-K is deemed not timely filed. The Form 10-K or other filing should be amended immediately to: (a) remove the non-registered auditor’s report, and (b) label the columns of the financial statements as “not audited.” The issuer would then need to file another amendment to file financial statements audited by a registered firm.

CHAPTER 13.

TENDER OFFERS AND EXCHANGE OFFERS

A. Introduction

In a tender offer, the bidder goes directly to the shareholders of the target company with an offer to buy their shares. Each shareholder individually decides whether or not to tender with (“friendly”) or without (“hostile”) the cooperation of the target’s board of directors. In contrast, a merger is a collective voting decision where the acquiror acquires the entire company if the target’s shareholders approve the merger. In a merger, the acquiror generally needs the approval of the target’s board of directors to present the transaction for a shareholder vote, which is not the case in a tender offer. There are two types of tender offers, “cash tender offers” and “exchange offers” (each of which may be made either by the issuer of the securities sought or by a third party). A “cash tender offer” is a tender offer in which the consideration offered consists solely of cash. An “exchange offer” is a tender offer in which the consideration offered consists all or partly of securities.

The Exchange Act regulates tender offers as follows:

1. **Reporting Requirements.** Section 13(d) of the Exchange Act requires anyone who acquires more than 5% of a class of equity securities registered under Section 12 of the Exchange Act to report the acquisition and his intentions for the issuer of the securities. (See “Officer, Director and Shareholder Reporting – Schedules 13D and 13G: Beneficial Ownership Reports”).
2. **Disclosure Requirements for Registered Equity Securities.** Section 14(d) of the Exchange Act is the basic section that regulates tender offers. Under this section, the bidder must make appropriate disclosure before commencing the tender offer. Additionally, Section 14(d)(4) requires disclosure by anyone making a solicitation or recommendation to the holders of the target’s securities to accept or reject a tender offer. Under Sections 14(d)(5), (d)(6) and (d)(7) and related SEC rules, a tender offer subject to Section 14(d) must comply with certain procedural and substantive requirements described below. Rule 14e-2 under the Exchange Act requires the target’s management to disclose its position on the tender offer, which disclosure in turn triggers the target’s obligation to file a Schedule 14D-9.
3. **Anti-Fraud and Substantive Provisions for All Securities.** Section 14(e) of the Exchange Act is an anti-fraud provision that makes it unlawful for any person making a tender offer (or defending against one) to make a false statement of material fact or misleading omission of material fact, or to engage in any fraudulent, deceptive or manipulative act or practice, in connection with any tender offer. Additionally, the SEC has adopted rules under Section 14(e), described below, which provide certain procedural and substantive requirements.

B. What is a Tender Offer?

“Tender Offer”. A “tender offer” is generally thought to be an offer to purchase that is made “publicly,” to all or substantially all of the shareholders of a corporation. However, it is not defined in the Exchange Act. The courts define the term “tender offer” on a case-by-case basis, and a broad definition will be used so as to effectuate the purposes of the Exchange Act

and its tender offer provisions (i.e., protection of the public and of investors). Consequently, all of the relevant facts must be considered in determining whether a tender offer exists.

1. Eight-Factor Test. Most courts refer to the eight-factor test given in *Wellman v. Dickinson*. However, not all eight factors need be present for the court to find a tender offer.

- (a) Was there an active and widespread solicitation of shares by the offeror?
- (b) Was the solicitation for a substantial percentage of the outstanding stock?
- (c) Was a premium price offered over the market price before the offer?
- (d) Were the terms of the offer firm and fixed?
- (e) Was the offer contingent on the tender by shareholders of a fixed minimum number of shares?
- (f) Was the offer to shareholders open for only a limited time?
- (g) Was there pressure put on shareholders to sell?
- (h) Were there public announcements accompanying the offer?

2. Hanson Trust “Totality of [the] Circumstances” Test. In the *Hanson Trust* case, the Second Circuit declined to elevate *Wellman* to a “litmus test,” and stated that the question “whether a solicitation constitutes a ‘tender offer’ within the meaning of [Section] 14(d) turns on whether, viewing the transaction in the light of the totality of [the] circumstances, there appears to be a likelihood that unless the pre-acquisition filing strictures of [Section 14(d)] are followed there will be a substantial risk that solicitees will lack information needed to make a carefully considered appraisal of the proposal put before them.”

3. Acquisitions Over a Stock Exchange. Normally, acquisitions made over a stock exchange in normal market transactions would not be a tender offer. However, under appropriate circumstances (for example, if the eight-factor test of *Wellman* were met), open-market purchases could amount to a tender offer.

4. Privately Negotiated Purchases. Similarly, although privately negotiated purchases ordinarily do not constitute a tender offer, under appropriate circumstances (for example, when enough of the *Wellman* factors are present, or when the “totality of [the] circumstances” so dictates) privately negotiated purchases may amount to a tender offer.

5. Alternative Test for Open Market and Privately Negotiated Purchases. Still another test, broader than the eight-factor test of *Wellman* and designed to apply to open market and privately negotiated purchases, was applied by the court in *S-G Securities, Inc. v. Fuqua Investment Co.* Under the *S-G Securities* test, a tender offer is present if there is:

- (a) a publicly announced intention by the purchaser to acquire a substantial block of the target’s stock, for the purpose of acquiring control of the target; and

(b) a subsequent rapid acquisition by the purchaser of large blocks of stock through open market and privately negotiated purchases.

C. Tender Offer Rules for Registered Equity Securities: Section 14(d)

1. Section 14(d) of the Exchange Act and its related rules apply to tender offers for any class of equity securities registered under Section 12 of the Exchange Act that, if successful, would result in the bidder beneficially owning more than 5% of the class of securities tendered. If Section 14(d) applies, Regulation 14D requires the following:

(a) Pre-Commencement Communications. Communications concerning a contemplated tender offer may be distributed before commencement of a tender offer. However, generally, the communication must be filed with the SEC on the date of first use.

(b) When a Tender Offer Commences. A tender offer commences when the bidder first publishes or sends or gives to security holders of the target the means of tender, i.e., the transmittal form or a statement of how it may be obtained. This is true even if there is no current offer by the bidder to purchase securities.

(c) Disclosure of Information. The bidder and target must make the following disclosures in connection with the tender offer:

- (i) Schedule TO. A bidder must file Schedule TO with the SEC (with copies delivered to the target, competing bidders and all national securities exchanges on which the target's stock is traded) when the tender offer commences.

The disclosures required by Schedule TO include:

- (A) a plain English summary term sheet;
- (B) target company identifying information;
- (C) identity and background of the bidder;
- (D) terms of the transaction;
- (E) past contacts, transactions, negotiations and agreements with the target;
- (F) purposes of the transaction and plans or proposals;
- (G) source and amount of funds or other consideration;
- (H) persons retained, employed, or to be compensated in connection with the offer;
- (I) if material to a decision by a potential tendering shareholder, financial statements of the bidder(s);

- (J) if material to a decision by a potential tendering shareholder, certain additional information about: the relationships between the bidder, the target, and their respective executive officers and directors; regulatory and antitrust issues affecting the transaction; applicability of the margin regulations (governing the use of securities as collateral for loans); and pending litigation affecting the offer; and
 - (K) such additional material information, if any, as may be necessary to make the required statements not materially misleading.
- (ii) Disclosure and Publication of Tender Offer Documents. In addition to filing the Schedule TO, the bidder must (both as a practical and a legal matter) take steps to inform the public of the offer. In addition to satisfying a disclosure requirement, the offer is generally deemed to commence on the date the means to tender are first published, sent or given to shareholders. Typically, this will happen in one of two ways: long-form publication or summary publication.
 - (A) Long-Form Publication. Long-form publication essentially requires the bidder to publish the offer (which must include or summarize the Schedule TO) in a newspaper of general circulation. Because this produces a rather lengthy (and expensive) advertisement, it is rarely used.
 - (B) Summary Publication. Summary publication consists of a short advertisement, similar to a “tombstone” ad that gives the essential terms of the offer and states where copies of the complete offer materials may be obtained.
- (iii) Target’s Recommendation. Regulation 14D also regulates the disclosure required in the target’s recommendation and its dissemination to shareholders.
- (d) Substantive Requirements. In addition to requiring disclosure, Section 14(d) and related rules also impose substantive requirements on tender offers, intended to ensure minimum standards of fairness and to curb abuses.
 - (i) Withdrawal Right. The offeree may change his mind and withdraw the securities that he tendered and deposited with the offeror at any time while the offer remains open.
 - (ii) Pro-Rationing in a Partial Tender Offer. Where the bidder seeks to purchase less than all the outstanding shares of a class and a greater number of shares are offered than the bidder intends to

purchase, it must purchase shares pro rata from each person who tenders.

- (iii) Opening the Offer Equally to All Security Holders: the “All Holders” Requirement. A tender offer must be open to all holders of the securities for which the offer is made.
- (iv) Equal Treatment of All Security Holders in the Price Paid For Their Securities: the “Best Price” Requirement. The consideration paid to any security holder in the offer must be the highest consideration paid to any other holder during the offer.
- (v) Limited Subsequent Offering Period. After the initial offering period has expired, a third-party bidder may provide a subsequent offering period of 3 to 20 business days after the successful completion of a tender offer during which security holders can tender their securities into the offer without withdrawal rights.

(e) Offers Requiring Registration Under the Securities Act. Where a tender offer involves the public offer of the bidder’s securities to the target’s shareholders, the bidder must also register the subject securities under the Securities Act (unless an exemption applies). In that case, the bidder must file both Schedule TO and the appropriate Securities Act registration form with the SEC, and must distribute both the tender offer documents and the prospectus for the securities offered to the shareholders of the target.

2. Exemptions. The tender offer rules under Section 14(d) do not apply to the following situations:

(a) 5% Limitation. Section 14(d) is not applicable if, after consummation of the offer, the person making the offer is not the beneficial owner of more than 5% of the class of equity security tendered.

(b) Equity Securities. Only equity securities registered under Section 12 of the Exchange Act are covered by Section 14(d), i.e., registered common stock, as opposed to debt securities, or bonds.

(c) Offers Made by an Issuer for Its Own Securities. Offers made by an issuer for its own securities are not covered by Section 14(d) but are covered by the issuer self-tender rule (Rule 13e-4 under the Exchange Act).

D. Tender Offer Rules for All Securities: Section 14(e)

Section 14(e) of the Exchange Act and its related rules apply to tender offers for any security regardless of whether it is an equity security or registered under Section 12 of the Exchange Act. Section 14(e) of the Exchange Act is a broadly-worded, anti-fraud provision that prohibits any person from making material false statements or misleading omissions, and from engaging in any fraudulent, deceptive or manipulative acts or practices, in connection with a tender offer or a solicitation of security holders in opposition to or in favor of a tender offer. If

Section 14(e) applies, Regulation 14E requires that the following conditions be met:

1. Duration. The bidder must keep its offer open for at least 20 business days from the date the tender offer commences. The offer must also remain open for at least 10 business days from the date that notice is first published, sent or given to security holders of any change in the percentage of the class of securities being sought, in the consideration offered or in the dealer's soliciting fee. The minimum time period an offer must remain open following material changes in the terms of the offer or in information concerning the offer (other than a change in the percentage of the class of securities being sought, in the consideration offered or in the dealer's soliciting fee) will depend on the facts and circumstances, including the relative materiality of the terms or information and the nature of the dissemination required.

2. Prompt Payment or Return of Tendered Securities. The bidder must pay the consideration offered or return the securities deposited by security holders promptly after the termination of the tender offer, which generally means no later than the third business day after the date of the transaction.

3. Target Company Recommendations. Within 10 business days from the date the bidder's tender offer commences, the target company must publish, send or give to security holders a statement of its position, disclosing whether it: (a) recommends accepting or rejecting the bidder's tender offer, (b) expresses no opinion and is remaining neutral, or (c) is unable to take a position concerning the bidder's tender offer. The statement must also include the reasons for the target's position (including its inability to take a position).

4. Insider Trading Prohibited: Disclose or Abstain from Trading. Under Rule 14e-3 under the Exchange Act, any person who possesses material information concerning a tender offer or proposed tender offer by another person is prohibited from trading in (or causing a trade in) target securities (or any securities convertible into or exchangeable for those securities, or any option or right to obtain or dispose of any of those securities) if: (a) the bidder has commenced or taken a substantial step to commence a tender offer, and (b) the person who possesses the information knows or has reason to know that the information is non-public and was acquired from the bidder, the target, or any person acting on their behalf, unless the information and its source are publicly disclosed within a reasonable time before the trade. This prohibition does not apply to: (a) a non-natural person (e.g., a broker-dealer) that shows that the individuals making the investment decision on its behalf did not know the material, non-public information and that it implemented policies and procedures, reasonable under the circumstances, taking into consideration the nature of its business, to ensure that individuals making investment decisions would not violate the prohibition; (b) purchases by a broker or another agent on behalf of the bidder; and (c) sales by any person to the bidder.

5. No Purchases Outside the Offer. Under Rule 14e-5 under the Exchange Act, in a tender offer for equity securities, the bidder is also prohibited from purchasing any securities of the class tendered and any related securities outside the tender offer. This provision is intended to prevent the bidder from manipulating the market price during the offer or from giving a person selling outside the offer a different deal than that received by persons tendering shares into the offer. However, certain transactions are exempt from Rule 14e-5. Some of these exemptions are discussed in E.4. below.

6. No False Announcements. A bidder is prohibited from publicly announcing plans to make a tender offer: (a) without an intent to commence the offer within a reasonable time and complete the offer, (b) with the intent to manipulate the price of the bidder's or target's securities, or (c) without a reasonable belief that the bidder will have the means to purchase the securities sought in the offer.

E. Cross-Border Tender Offers and Exchange Offers for a Foreign Target – Tier I and Tier II

The exemptions for cross-border tender and exchange offers for the securities of foreign private issuers are designated Tier I and Tier II. Neither of the exemptions relieves issuers, third party bidders or other persons from the anti-fraud, anti-manipulation or civil liability provisions of the U.S. securities laws, including Sections 10(b) and 14(e) of the Exchange Act and Rules 10b-5 and 14e-3 thereunder. (Rule 10b-5 is discussed in Chapter 14.)

1. Tier I. The Tier I exemption provides a sweeping exemption from U.S. tender offer (both issuer and third party) and going-private regulation so long as:

- (a) the target is a foreign private issuer;
- (b) U.S. holders own 10% or less of the class of securities sought in the tender offer;
- (c) U.S. holders participate in the offer on terms at least as favorable as those offered to any other holders subject to several exceptions, described below;
- (d) bidders provide U.S. security holders with the tender offer circular or other offering document, in English, on a comparable basis to that provided to other security holders; and
- (e) bidders that would otherwise have to file a tender offer statement (Schedule TO and Regulation 14D) with the SEC must submit (rather than file) an English language translation of the offering materials to the SEC under cover of Form CB and, in the case of a foreign offeror, file a consent to service of process on Form F-X. Also, the target company may, in lieu of filing its response under Schedule 14D-9, submit its home jurisdiction response materials under cover of Form CB.

The nationality of the bidder does not matter. U.S. bidders may rely on the exemption. The target must be a foreign private issuer and not an investment company (other than a registered closed-end investment company).

A Tier I tender offer that meets certain additional requirements (as described below) is also exempt from Rule 14e-5, which generally prohibits a bidder in a tender or exchange offer from purchasing the subject security outside the offer.

The equal treatment requirement (discussed in C.1.(d)(iv) above) mandates not only equal type and amount of consideration, but also equality in procedural terms of the tender

offer (e.g., duration, pro-rationing and withdrawal rights). There are several exceptions to the equal treatment requirement:

(a) Cash-Only Exception. In an exchange offer, U.S. holders may be offered only cash if the bidder has a reasonable basis to believe that the cash is substantially equivalent to the value of the securities and any cash or other consideration offered to non-U.S. holders. To ensure equivalent value, if the offered security is not a “margin security” under Regulation T, the offeror must provide (upon the request of the SEC or a U.S. security holder) an opinion from an independent expert stating that the cash-only consideration is substantially equivalent to the securities and any cash or other consideration offered outside the United States. If the offered security is a margin security, no opinion is needed. Instead, the bidder must provide (upon the request of the SEC or a U.S. security holder), information on recent trading prices of the offered security. Specifically, the bidder must provide the closing price and daily trading volume of the offered security on the principal trading market for the security as of the last trading day of each of the six months preceding the announcement of the offer and each of the trading days thereafter.

(b) Blue Sky Exceptions. In an exchange offer, the offeror may also exclude U.S. holders in any U.S. state or jurisdiction that: (i) does not have an applicable blue sky exemption from registration or qualification (for an offer exempt from Securities Act registration under Rule 802, which is discussed below); or (ii) does not register or qualify the offer after a good faith effort by the offeror to do so (for an offer registered under the Securities Act). However, in both cases the offeror must offer those security holders cash consideration instead of excluding them, if it has offered cash consideration to security holders in another state or jurisdiction (whether inside or outside the United States).

(c) Loan Notes Exception. If the bidder offers “loan notes” solely to offer sellers tax advantages not available in the United States and the notes are neither listed on any organized securities market nor registered under the Securities Act, the bidder need not offer loan notes to U.S. holders. “Loan notes” are short-term notes that may be redeemed in whole or in part for cash at par on any interest date in the future. Common in the United Kingdom (“U.K.”), loan notes are intended to defer the recognition of income and capital gains on the sale of securities under foreign tax laws. Because this tax benefit is not available to U.S. security holders, a bidder need not offer loan notes to U.S. security holders.

2. Tier II. The Tier II exemption provides relief from selected provisions of the U.S. tender offer rules for issuer and third-party tender offers when the subject company is a foreign private issuer (and not an investment company, other than a registered closed-end investment company) and U.S. security holders own no more than 40% of the class of securities sought in the tender offer. As with Tier I, the bidder’s nationality does not matter. The exemptions address a number of provisions that frequently conflict with home jurisdiction regulations (principally the U.K. Takeover Code), and from which the SEC staff has from time-to-time granted relief on a case-by-case basis. Qualifying offers receive relief from Exchange Act requirements concerning: (a) equal treatment of target security holders (the “all holders” and “best price” requirements); (b) notice of extensions of the offer; (c) prompt payment for or return of tendered securities; (d) subsequent offering period withdrawal rights; (e) payment of interest on securities tendered during a subsequent offering period; (f) withdrawal rights while tendered

securities are being counted; (g) mix and match elections and the subsequent offering period; (h) early termination of an initial offering period; and (i) withdrawal rights after reducing or waiving a minimum acceptance condition. The Tier II bidder must comply with the remaining tender offer provisions, including the procedural, disclosure and filing requirements. U.S. tender offer documents (e.g., Schedule TO), rather than Form CB, must be used in a Tier II tender offer. Additionally, Tier II transactions are not exempt from the “going private” provisions of Rule 13e-3 under the Exchange Act.

3. Eligibility Threshold - Calculating U.S. Ownership

(a) Negotiated Transactions

Eligibility to rely on the cross-border exemptions is determined by the percentage (up to 10% or up to 40%) of the relevant class of target securities held by U.S. beneficial owners. Any securities held by the acquiror in a business combination transaction are excluded from the calculation of U.S. ownership. As revised in 2008, the rules no longer exclude securities held by individual holders of more than 10% of the subject class from the calculation of U.S. ownership. To identify those securities held for the accounts of persons located in the United States, the rules require the acquiror in a negotiated transaction to “look through” securities held of record by banks, broker-dealers and other nominees located in: (i) the United States; (ii) the subject company’s jurisdiction of incorporation or that of each participant in a business combination; and (iii) the jurisdiction that is the primary trading market for the subject securities, if different than the subject company’s jurisdiction of incorporation. However, if after “reasonable inquiry” the acquiror is unable to obtain information about the location of the security holders for whom a nominee holds, it may assume that the holders are residents of the jurisdiction in which the nominee has its principal place of business.

Acquirors must calculate U.S. ownership in the target company as of any date no more than 60 days before and no more than 30 days after the public announcement (instead of commencement) of the cross-border tender offer or business combination transaction. However, if the issuer or acquiror is unable to complete the look-through analysis in this 90-day period, it may use a date within 120 days before public announcement (although this extended period is not available for rights offerings).

(b) Alternate Test

The rules provide for an alternate test to determine eligibility to rely on the cross-border exemptions. The alternate test is available for all non-negotiated (i.e., “hostile”) transactions and in negotiated transactions where the issuer or acquiror is unable to conduct the look-through analysis.

Whether an issuer or acquiror is unable to conduct the required look-through analysis is a question of facts and circumstances, but the need to dedicate time and resources to the analysis, or concerns about completeness and accuracy of the information gathered, are not adequate justification for using the alternate test. Examples of when the alternate test may be used are: (i) where security holder lists are only generated at fixed intervals, are out of date and more current information is not otherwise available; (ii) when the subject

securities are in bearer form; and (iii) when nominees are prohibited by law from disclosing information about the holders.

The new, alternate test replaces what was called the “hostile presumption” in the old rules for non-negotiated transactions. Under the alternate test, a third-party bidder in a non-negotiated tender or exchange offer may assume that U.S. ownership in the target company is no more than 10% or 40% so long as:

- (i) average daily trading volume of the subject securities in the United States does not exceed 10% or 40% of the average daily trading volume worldwide over a 12-month period ending no more than 60 days before the public announcement of the transaction; and
- (ii) the bidder has no reason to know, before the public announcement of the offer, that actual U.S. ownership is inconsistent with that figure (either based on the issuer’s annual filings with the SEC or foreign regulators made before public announcement of the transaction or based on the bidder’s actual or imputed knowledge from other sources).

For an acquiror in a negotiated transaction to rely on the alternate test, the subject securities must also have a “primary trading market” outside the United States, meaning that at least 55% of the trading volume in the subject securities takes place in one foreign jurisdiction (or two, if the trading in at least one of the foreign jurisdictions is larger than the trading in the United States) during a recent 12-month period. The primary trading market requirement does not apply to the alternate test in non-negotiated transactions.

Under the second element of the alternate test (i.e., (ii) above), an acquiror must consider information that the acquiror knows or has “reason to know” that U.S. beneficial ownership exceeds 10% or 40% as applicable. This element of the alternate test provides that the applicable cross-border exemption will not be available and the acquiror will be deemed to know information about U.S. ownership of the subject class that: (A) is publicly available and appears in any filing with the SEC or any regulatory body in the issuer’s jurisdiction of incorporation or (if different) the non-U.S. jurisdiction in which the primary trading market for the subject securities is located; (B) is available from the issuer; (C) is publicly available from sources reasonably accessible at a low cost, if the sources are reasonably reliable; or (D) is obtained from a third-party information provider and other advisers engaged by the parties to the transaction that have provided information about U.S. ownership. However, this does not require the issuer or acquiror to engage these third parties, only that the acquiror take into account information obtained from a third-party information provider. The examples listed in (A) through (D) above are not exclusive; an acquiror may have “reason to know” information from other sources, depending on the particular facts and circumstances of the transaction. However, information acquired after public announcement will not disqualify an acquiror from relying on the cross-border exemptions.

4. Rule 14e-5

(a) Tier I and Tier II Offers

Generally, Rule 14e-5 under the Exchange Act prohibits a bidder, its affiliates and certain persons acting on their behalf in a tender or exchange offer from purchasing target equity securities outside the offer. Tier I tender offers are generally exempt from Rule 14e-5 if, in addition to meeting the Tier I requirements described above (and the requirements of the “home jurisdiction,” as defined below):

- (i) the offering documentation provided to U.S. security holders prominently discloses the possibility of purchases outside the tender offer and the manner in which any information about such purchases will be disclosed; and
- (ii) the bidder discloses in the United States information about these purchases in a manner comparable to the disclosure it makes in the home jurisdiction. (As used here, “home jurisdiction” means both the jurisdiction of the issuer’s incorporation, organization or chartering and the principal foreign market where the issuer’s securities are listed or quoted.)

The exemption from Rule 14e-5 also covers Tier II transactions, subject to certain conditions intended to promote the fair treatment of tendering security holders, for: (i) purchases or arrangements to purchase pursuant to a foreign tender offer(s) where the offeror seeks to acquire subject securities through a U.S. tender offer and a concurrent or substantially concurrent foreign offer(s); and (ii) purchases or arrangements to purchase by an affiliate of a financial adviser and an offeror and its affiliates that are permissible under and conducted in accordance with the laws of the subject company’s home jurisdiction.

(b) All Tender Offers

In a tender offer for the securities of a foreign private issuer, purchases by “connected exempt market makers” and “connected exempt principal traders” under the U.K. City Code on Takeovers and Mergers are generally exempt from Rule 14e-5 (subject to certain additional requirements).

5. Rule 802. Rule 802 under the Securities Act provides an exemption from registration for offerings of securities in exchange for the securities of foreign private issuers in an exchange offer or business combination. The exemption does not relieve issuers, third-party bidders or other persons from the anti-fraud, anti-manipulation or civil liability provisions of the U.S. securities laws.

Rule 802 provides an exemption from Securities Act registration for offers and sales in any exchange offer for a class of securities of a foreign private issuer or in any exchange of securities for the securities of a foreign private issuer in any business combination if the U.S. holders of the foreign subject company hold no more than 10% of the securities that are the subject of the exchange offer or business combination. The Rule 802 exemption is available to

both U.S. and foreign bidders, regardless of the reporting status of the bidder and regardless of whether the bidder is the issuer of the securities being offered or a third-party bidder. For the exemption to apply, U.S. holders must participate in the exchange offer or business combination on terms at least as favorable as the other holders of the subject securities (subject to one exception). Under this exception, where a U.S. state or jurisdiction does not provide an exemption comparable to Rule 802, thereby requiring registration or qualification, the offeror may exclude security holders in that state or jurisdiction if a cash-only alternative is not being offered in any other state or jurisdiction (whether inside or outside the United States). However, if a cash-only alternative is being offered anywhere, the offeror must offer the same cash-only alternative to security holders in any U.S. state or jurisdiction that would require registration or qualification. The Rule 802 exemption is not conditioned on delivery of any specific form of disclosure documents. However: (a) if the offeror disseminates any information concerning the exchange offer or business combination to security holders in the foreign subject company's home jurisdiction, the offeror must disseminate that information to U.S. security holders in English on at least a comparable basis; and (b) if the offeror disseminates the information solely by publication in the offeror's home jurisdiction, it must publish that information in the United States in a manner reasonably calculated to inform U.S. security holders of the offer. This information must also be submitted in English on Form CB to the SEC along with, in the case of a foreign offeror, a Form F-X consent to service of process. Thus, instead of filing a registration statement on Form S-4, S-1, F-4 or F-1, an offeror relying on Rule 802 will submit Form CB and, if a foreign company, file Form F-X, which are much less burdensome to prepare than a registration statement. (A legend must be included in any information the offeror disseminates to U.S. security holders stating, among other things, that the exchange offer or business combination is being conducted under foreign disclosure requirements, and that those requirements may differ from U.S. disclosure requirements, including financial statement requirements.)

The Rule 802 exemption covers only the issuer of the securities and the transaction in which the securities are exchanged. It does not provide an exemption to affiliates or others for resales of the issuer's securities. Securities acquired in a Rule 802 transaction are "restricted securities" if the securities for which they were exchanged were restricted securities in the hands of the holders. Conversely, the securities are unrestricted (and thus freely tradable), if the securities for which they were exchanged were unrestricted, except by affiliates of the issuer in whose hands they will constitute control stock.

6. Blue Sky Compliance. There is no general exemption from state blue sky laws that parallels Rule 802. Therefore, issuers must ensure that they consider the effect of blue sky laws before relying on Rule 802. However, federal regulation has preempted state registration requirements to the extent that the offered securities are listed on the NYSE, the NYSE Amex, the NASDAQ Global Market or any national securities exchange (or tier or segment of it) that the SEC by rule determines has substantially similar listing standards (e.g., the NASDAQ Capital Market).

F. The MJDS and Tender Offers

1. Requirements. For tender offers for Canadian targets, the MJDS provides relief from the U.S. tender offer rules. The target must be a Canadian foreign private issuer, with less

than 40% of its stock held in the United States. A third-party bidder is entitled to rely on a conclusive presumption that the target is a foreign private issuer and that U.S. holders hold less than 40% of the subject class of securities unless: (a) the bidder has actual knowledge to the contrary, (b) the target's most recent annual report or annual information form publicly filed in the United States or Canada indicates that U.S. holders hold 40% or more, or (c) the aggregate (published) trading volume of the subject class on all U.S. national securities exchanges (including NASDAQ) exceeded the aggregate (published) trading volume of that class on all Canadian securities exchanges and the Canadian Dealing Network, Inc. ("CDN") over the 12 calendar month period immediately preceding commencement of the third-party tender offer (or, if the third-party tender offer is commenced in response to a prior offer, the 12 calendar month period immediately preceding commencement of the initial offer). The offer must comply with Canadian tender offer rules, and the bidder must not obtain any regulatory relief from Canadian requirements that provide protections similar to those provided by the U.S. tender offer rules. Bidders of any nationality may rely on the MJDS for cash tender offers. However, only Canadian issuers may use the MJDS for exchange offers.

2. Share Ownership – Competing Bids. Once an offer is commenced under the MJDS, competing bidders may also use the MJDS, even if the target's U.S. ownership goes to or above 40%, as sometimes happens when U.S. arbitrageurs become involved, or if the original bid was made under the MJDS in reliance on the presumption based on trading volume, and actual U.S. ownership turned out to be 40% or greater. In other words, the MJDS provides that the date of the first bid made under the MJDS is also the date for determining the percentage of U.S. holders for all subsequent bids. Actually, subsequent competing bids are able to look back to the initial commencement date so long as the initial offer was *eligible* to use the MJDS, regardless of whether the initial offer took advantage of the MJDS.

3. Dissemination and SEC Filing. Tender offer materials are prepared under Canadian requirements and, if the target's securities are equity securities registered under the Exchange Act, are filed with the SEC under cover of Schedule 14D-1F (for a third-party bidder). (Specifically, if the bidder complies with the laws, regulations and policies of at least one Canadian jurisdiction governing the conduct of the tender offer, the offer is deemed to have met the requirements of Sections 14(d)(1) through 14(d)(7) of the Exchange Act, Regulation 14D and Schedules TO and 14D-9 thereunder and Rule 14e-1 of Regulation 14E under the Exchange Act. However, to satisfy the Exchange Act, the complete disclosure documents required to be furnished to target shareholders must be filed with the SEC on Schedule 14D-1F and disseminated to target shareholders residing in the United States in accordance with the laws, regulations and policies of that Canadian jurisdiction.) The target company's response is filed under Schedule 14D-9F. Schedule 14D-9F was adopted to permit a Canadian target issuer, and its directors and officers, to comply solely with the disclosure requirements of Canadian takeover laws during the course of an MJDS third-party tender offer. The filer of Schedule 14D-9F must: (a) file with the SEC and deliver to U.S. target security holders the entire disclosure document required to be delivered to target shareholders under Canadian law; (b) file with the SEC, as part of the Schedule, certain exhibits (but need not send these exhibits to target shareholders unless so required under Canadian laws, regulations or policies); (c) undertake to provide additional information to the SEC if so requested; (d) file an irrevocable consent to service of process and power of attorney on Form F-X (if the filer is a non-U.S. person); and (e) sign the Schedule 14D-9F in a specified manner (and thereby irrevocably consent that any administrative subpoena may

be served, or any administrative proceeding or civil action where the cause of action arises out of or relates to any offering made in connection with the filing of the Schedule, may be commenced against it in any administrative tribunal or court in the United States).

4. Exchange Offers. Where securities are offered, qualifying Canadian bidders may file MJDS Securities Act registration statements on Forms F-8 or F-80 (the MJDS exchange offer forms), or Form F-10 (the general, all-purpose MJDS form). The registration statement is effective upon filing and there is no SEC review, other than to check the bidder's eligibility to use the selected form.

5. Blue Sky Compliance. Where securities are offered, MJDS transactions must comply with state blue sky laws. The states have not adopted blanket exemptions for MJDS exchange offers. The states generally have adopted blanket "marketplace" exemptions for securities listed on the NYSE, the NYSE Amex or the NASDAQ Global Market (and in some states, securities listed on specified regional exchanges) and securities of the same issuer that are senior to securities so listed. However, these marketplace exemptions are no longer needed given federal preemption. For transactions that are not preempted, the securities must be registered or exempt in any state where holders of the target's securities reside. Most states have exemptions for transactions effected by shareholder vote, but not for exchange offers. State exemptions are not uniform, and must be reviewed on a state-by-state basis.

A 50-state blue sky filing can be costly and administratively burdensome. Additionally, the filings are not automatically effective, and the states reserve the right to review them before declaring them effective so the offer can be consummated. Many states have adopted procedures for expedited seven-day review of Form F-8 registration statements. Normally, states have not raised significant comments or caused delays, but the issuer can never be sure in advance that a state will not have significant comments or cause delay through slow processing of the filing. Accordingly, particularly in smaller deals, issuers seek to minimize the number of states in which they must file by seeking out exemptions.

6. Going Private Transactions. Unlike the Tier I exemption, the MJDS does not provide an exemption from the “going private” provisions of Rule 13e-3 under the Exchange Act.

G. Excluding U.S. Target Security Holders

Bidders in cross-border tender offers frequently seek to avoid the U.S. tender offer and registration rules. The SEC’s view is that offer structures that exclude U.S. security holders from offers for foreign targets (“exclusionary offers”) are inappropriate for U.S. bidders. The SEC stated that where the subject class is registered under Section 12 of the Exchange Act, and particularly, where the subject securities trade on a U.S. exchange, it will view exclusionary offers skeptically where the participation of those U.S. holders is needed to meet the minimum acceptance condition in the tender offer.

Whether U.S. tender offer rules apply to a cross-border tender offer depends on whether the bidder triggers U.S. jurisdictional means in making the tender offer. The SEC has provided guidance on measures bidders may take to avoid triggering U.S. jurisdictional means and, thereby, avoid application of the U.S. tender offer rules. Bidders who are not U.S. persons may structure a tender offer for target securities of a foreign private issuer and exclude U.S. target security holders if the offer is conducted outside the United States and U.S. jurisdictional means are not implicated. However, a bidder may implicate U.S. jurisdictional means if it fails to take adequate measures to prevent tenders by U.S. target security holders while purporting to exclude them. When a bidder permits U.S. target security holders to participate in a tender offer, it must follow U.S. rules unless an exemption applies. It is important that bidders do not purport to exclude U.S. holders while still accepting their tenders.

Bidders seeking to avoid the application of U.S. law should take special precautions to assure that their offer is not being made in the United States. The most basic measure is to include legends on the offer materials and on any Internet web site on which they are posted, indicating that the offer is not being made in the United States. The bidder should take precautions to assure that tenders are not accepted from, nor sales of bidder securities made (in the case of exchange offers) to, target security holders resident in the United States. These may include, in responding to inquiries and processing letters of transmittal, obtaining adequate information to determine whether the target security holder is a U.S. investor. Additionally, the bidder could require a representation by the tendering security holder, or anyone tendering on that person’s behalf, that the person tendering is not a U.S. holder or someone tendering on behalf of a U.S. holder. When disseminating cash or securities to tendering holders, special care should be taken to avoid mailing into the United States.

Where tenders in exclusionary offers are made through offshore nominees, bidders could require that these nominees certify that tenders are not being made on behalf of U.S. holders. However, this may be problematic where the law of the applicable foreign jurisdiction prevents the nominee from knowing the identity or location of beneficial owners on whose behalf they hold.

H. Vendor Placements

In many business combination transactions, the offer consideration may include securities of the bidder. In cross-border exchange offers, bidders may seek to avoid the registration requirements of the Securities Act by establishing a vendor placement arrangement for the benefit of U.S. target security holders who tender into the offer. In a vendor placement, the bidder employs a third party to sell offshore the securities that would be issued in the offer to tendering U.S. security holders. The bidder (or the third party) then remits the proceeds of the resale (minus expenses) to those U.S. target security holders that tendered into the offer. In effect, the vendor placement is an effort to convert an exchange offer involving the offer and sale of the bidder's securities (which would require Securities Act registration) into an offer involving solely cash (which does not require registration) for tendering U.S. security holders. In a vendor placement, U.S. holders are not excluded from participating in the offer but they participate on terms different from those afforded other target security holders.

Although tendering U.S. holders receive cash in a vendor placement, the amount of cash received is largely dependent on the market value of the securities sold. The protections of the Securities Act are intended to give investors access to information when making an investment decision for the purchase of a security. A vendor placement does not in all circumstances eliminate the requirement for Securities Act registration, because tendering U.S. holders may be effectively making an investment decision for the purchase of a security.

The SEC believes that a vendor placement arrangement in a cross-border exchange offer would be subject to Securities Act registration unless the market for the bidder securities to be issued in the exchange offer and sold under the vendor placement procedure is highly liquid and robust and the number of bidder securities to be issued for the benefit of tendering U.S. holders is relatively small compared to the total number of bidder securities outstanding. The SEC also considers:

- (a) whether sales of bidder securities through the vendor placement process are made within a few business days of the closing of the offer;
- (b) whether the bidder announces material information, such as earnings results, forecasts or other financial or operating information, before the sales process is complete; and
- (c) whether the vendor placement involves special selling efforts by brokers or others acting on behalf of the bidder.

These factors are important because they indicate whether the market price that U.S. investors will receive when bidder securities are sold on their behalf is representative. The factors also are intended to ensure that rather than making an investment decision, U.S. holders are making a decision to tender their target securities for an amount of cash that although not fixed, can be readily estimated based on historic trading prices.

In tender offers subject to Section 14(d) of the Exchange Act, the all holders and best price requirements in Rule 14d-10 under the Exchange Act are implicated by the use of the vendor placement structure because U.S. target security holders would receive different

consideration from their non-U.S. counterparts. Generally, the SEC believes that the parameters of the Tier I cross-border exemption should represent the appropriate limits under which a bidder in a tender offer subject to Regulation 14D may offer cash to U.S. security holders while issuing shares to their counterparts outside the United States. In Tier I tender offers, for purposes of complying with the equal treatment requirement, bidders are permitted to offer cash consideration to U.S. holders in lieu of offering securities so long as the bidder has a reasonable basis for believing that the amount of cash is substantially equivalent to the value of the consideration offered to non-U.S. holders.

Bidders making a cross-border exchange offer sometimes seek to exclude some U.S. target holders and include in the exchange offer only those U.S. target holders (such as institutional investors) for whom an exemption from the registration requirements of the Securities Act may be available. The SEC has stated that exchange offers for securities subject to Section 14(d) of the Exchange Act may not be made in the United States on a private offering basis, consistent with the all holders provisions of Rule 14d-10. Thus, even where the bidder is eligible to rely on an exemption from Section 5 of the Securities Act for such offers, it would violate the equal treatment provisions applicable to such offers by excluding target security holders for whom an exemption was not available. Similarly, as discussed above, offering cash under a vendor placement arrangement to some U.S. holders and bidder securities to others (such as institutions) is not permitted in tender offers subject to the all holders rule.

Where a bidder seeks to use the vendor placement structure for a tender offer subject to Rule 14d-10 at U.S. ownership levels above Tier I, it must seek an exemption from those rules, which is granted only where it is in the interests of U.S. investors (i.e., rarely). Thus, it is not advisable to conduct vendor placements in a Tier II transaction.

I. Complying with U.S. Tender Offer Rules

Where neither the MJDS nor the Tier I exemption for cross-border tender offers provides relief, tender offers for a class of securities registered under the Exchange Act must comply with the filing, disclosure and procedural requirements of the SEC's tender offer rules.

Where the bidder will issue securities and no exemption from Securities Act registration is available, the bidder must register the exchange offer or business combination under the Securities Act. A foreign bidder will normally register an exchange offer or business combination using Form F-4, unless the MJDS is available.

Form F-4 registration statements filed in exchange offers and business combinations are subject to SEC review, and the offer or combination may not be consummated until the SEC's review and comment process is completed.

In the absence of a listing of the bidder's shares on a specified U.S. exchange or some other exemption, registration under state blue sky laws is also required. State regulators may feel freer to comment on Form F-4 filings than on MJDS filings, raising the possibility of a more burdensome and lengthy state review process.

CHAPTER 14.

FRAUD IN THE PURCHASE OR SALE OF SECURITIES: RULE 10b-5

A. Introduction

Rule 10b-5 under Section 10(b) of the Exchange Act is the most commonly invoked remedy in private securities litigation. The Rule is as follows:

Rule 10b-5: Employment of Manipulative and Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

- (a) To employ any device, scheme, or artifice to defraud,
- (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
- (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

The Rule is used in many situations, including: (a) when a corporation issues misleading information to the public, or keeps silent when it has a duty to disclose; (b) when a person mismanages a corporation in ways that are connected with the purchase or sale of securities; and (c) when a securities firm or another person manipulates the market for a security traded in the over-the-counter market or engages in certain other forms of conduct connected with the purchase or sale of securities. Another well known use of the Rule has been in insider trading cases, typically those in which a corporate insider trades in his company's securities when in possession of material, non-public information, or discloses such information to another person who uses it to trade.

B. Elements of a 10b-5 Action

1. **Purchase and Sale.** The conduct must be "in connection with the purchase or sale of [a] security."
2. **Reliance.** Plaintiff must demonstrate reliance on the alleged misconduct. Proof of a material misrepresentation or omission results in a presumption of reliance.
3. **Causation.** Plaintiff must demonstrate that but for the defendant's misconduct plaintiff's loss would not have occurred. In insider trading cases, proof of possession by defendant of inside information at the time of the trade, rather than actual use of the information, is sufficient to prove causation.

4. Standing. A private plaintiff must be a purchaser or seller of securities to have standing. However, privity with the alleged wrongdoer is not required.

5. Scienter. The alleged wrongdoing must be intentional or reckless. Negligent misrepresentation or omission is insufficient to support liability.

6. Materiality. The alleged misrepresentation or omission must be “material,” i.e., there must be a substantial likelihood that a reasonable investor would consider it important in making a decision to buy or sell a security.

Under the U.S. securities laws, information is generally deemed material if there is a substantial likelihood that a reasonable investor would consider it important in making a decision to buy or sell a security. While the SEC has consistently declined to provide a bright-line test of “materiality,” when it adopted Regulation FD the SEC enumerated events and circumstances that it believes should be carefully reviewed to determine whether or not they are material. The SEC stated that, while it is not possible to create an exhaustive list, the following items are some types of information or events that should be reviewed carefully to determine whether they are material:

- (a) earnings information;
- (b) mergers, acquisitions, tender offers, joint ventures or changes in assets;
- (c) new products or discoveries, or developments regarding customers or suppliers (e.g., the acquisition or loss of a contract);
- (d) changes in control or in management;
- (e) change in auditors or auditor notification that the issuer may no longer rely on an auditor’s audit report;
- (f) events regarding the issuer’s securities – e.g., defaults on senior securities, calls of securities for redemption, repurchase plans, stock splits or changes in dividends, changes to the rights of security holders and public or private sales of additional securities; and
- (g) bankruptcies or receiverships.

The SEC has emphasized that issuers should not assume that a misstatement or omission of items that falls below a certain quantitative threshold is immaterial and has indicated that an assessment as to materiality must include “the factual context.” Because determinations of materiality are very fact specific, they can require difficult judgments.

C. Damages and Penalties

Violations of Section 10(b) and Rule 10b-5 carry civil and criminal penalties. Generally, the measure of damages in private actions is out-of-pocket loss, measured by the difference between the price paid or received by the plaintiff and the actual value of the securities at the time of purchase or sale. The SEC may seek civil penalties of up to \$100,000 (for individuals)

and \$500,000 (for corporations), or disgorgement of any gains, whichever is greater.

Civil penalties in insider trading cases brought in federal court can be larger. The insiders may be responsible for their profits earned (or losses avoided) as well as those by their tippees. The SEC may recover from the insider up to three times the profit realized or the loss avoided as a result of insider trading. Additionally, the SEC may seek civil penalties of one million dollars or up to three times the profits realized or losses avoided, whichever is greater, from control persons, including officers and directors, who: (a) knew or recklessly disregarded the fact that the controlled person was likely to engage in the violation and failed to take “appropriate” steps to prevent the violation; or (b) knowingly or recklessly failed to establish, maintain or enforce any policy or procedure required under Section 15(f) of the Exchange Act or Section 204A of the Advisers Act if such failure substantially contributed to or permitted the occurrence of the violation. The SEC often refers egregious insider trading cases to the U.S. Department of Justice for criminal prosecution.

D. Statute of Limitations

A private 10b-5 action must be filed within two years after discovery of the facts constituting the violation and within five years after the violation. Civil enforcement actions may be brought by the SEC at any time.

E. Controlling Person Liability

Section 20 of the Exchange Act provides that controlling persons are jointly and severally liable for any violation of the Exchange Act or its rules by the company or other persons they control unless they acted in good faith and did not directly or indirectly induce the actions constituting the violation.

F. Insider Trading

Rule 10b-5 prohibits the use of material non-public information in securities transactions (“insider trading”) and the communication of such information to others who use it in securities trading (“tipping”). As discussed above, “material information” is information that a reasonable investor would consider important in making an investment decision (i.e., to buy, sell or hold a security), or that is reasonably certain to affect the price of the securities of the company to which it relates. “Non-public information” is generally information that has not been widely disseminated or disclosed to the general investing public for at least two business days.

The prohibition against insider trading extends to the following types of activities:

1. trading by “classic” insiders, e.g., officers, directors;
2. trading by “temporary” insiders, e.g., attorneys, auditors, bankers, etc., who obtain information about an issuer while performing their duties to the issuer;
3. trading by an individual who “misappropriates” information in violation of a duty owed to the source of the information (which may or may not be the issuer); and

4. trading by persons who receive information from insiders in breach of a duty owed by the insider to the issuer (i.e., “tippees”).

An issuer’s directors and senior management should not trade in the issuer’s securities at any time when the issuer itself would be barred from trading because material information concerning the issuer has not been made public. This statement also extends to any employee who in the course of a confidential relationship (i.e., his employment relationship) acquires material undisclosed information about the issuer, and to any other person to whom such information is subsequently disclosed.

Actions under Rule 10b-5 may be brought by the SEC or by persons claiming to have incurred damages as a result of selling to or buying from a person acting with knowledge of material non-public information.

CHAPTER 15.

LIABILITY AND ENFORCEMENT

A. Introduction

Failing to comply with the U.S. securities laws is punishable by civil and criminal penalties. Legal actions may be brought by private parties and government agencies. Remedies and sanctions for improper securities activities can be sought through civil litigation, administrative proceedings and criminal proceedings. These methods are not exclusive and a person could be forced to defend himself in multiple proceedings.

B. Securities Act Violations and Public Offerings

Any person who violates any provision of the Securities Act may be liable to the SEC for the greater of disgorgement of profits or penalties ranging from up to \$100,000 for individuals to \$500,000 for entities, for each violation. This includes issuers, underwriters or dealers who violate the registration requirements of Section 5 of the Securities Act. Persons who unlawfully sell unregistered securities in violation of Section 5 may also be subject to civil suits by purchasers of the securities under Section 12(a)(1) of the Securities Act for “rescission” (i.e., the purchase price plus interest, less income earned) or, if the plaintiff no longer owns the security, damages based on the difference between the purchase price and plaintiff’s resale price.

Section 11 of the Securities Act imposes liability for misleading disclosure in a registration statement, including the prospectus. The issuer, everyone who signed the registration statement, every director or partner, every person named (with his consent) as being or about to become a director or partner, every underwriter and every named expert (e.g., accountants, engineers) are subject to liability under Section 11. Generally, the plaintiff may recover the difference between the purchase price and either his resale price if he no longer owns the security or the price of the security when the suit was filed.

Section 12(a)(2) of the Securities Act provides a second basis for liability for misleading disclosure in a public offering against those who offer and sell the security, including those with a financial interest or who authorized the selling efforts, such as underwriters. If the plaintiff still owns the securities he can rescind the sale and recover the purchase price plus interest, less income earned. If the plaintiff no longer owns the securities, his damages are the depreciation in the value of the securities caused by the false statements or omissions.

An issuer will have almost no defense to an action brought under Section 11 of the Securities Act if there is a material misstatement in, or misleading omission from, its registration statement. No proof of fraud, intent or even negligence is required, and “due diligence” is not a defense. The only defense an issuer can assert in an action based on a misstatement or omission in a registration statement is that the person purchasing the security covered by the registration statement knew of the misstatement or omission at the time of the purchase and, therefore, was not in fact misled.

Unlike the issuer, a director or an officer who signs a Securities Act registration statement has the so-called “due diligence” defense to an action under Section 11 if he can

demonstrate that, after reasonable investigation, he had reasonable grounds to believe, and did believe, that the statements in the registration statement were true and that there was no material omission in the registration statement. The standard of reasonableness is that required of a prudent person in the management of his own property. Underwriters of an issuer's securities also have the due diligence defense to actions brought under Section 11 or Section 12(a)(2).

U.S. courts have uniformly held that indemnification by a U.S. issuer of its directors, officers and controlling persons against liabilities arising out of fraudulent misrepresentations in, or omissions from, the issuer's registration statement is unenforceable and contrary to public policy. Nevertheless, it is permissible under U.S. law for an issuer to obtain insurance against such liabilities.

C. Other Liability Provisions

Disclosure violations in public offerings may also trigger liability under Section 17(a) of the Securities Act and Rule 10b-5 under the Exchange Act, both of which are broad anti-fraud provisions that provide an array of remedies such as civil or administrative proceedings by the SEC, criminal liability and for Rule 10b-5, civil damage suits by private parties. Proof of "scienter" (i.e., intent, or at least reckless conduct) is required to establish liability under Rule 10b-5. While the language of Section 17(a) is very similar to that of Rule 10b-5, most actions under Section 17(a) do not require proof of scienter to establish liability. Instead, a showing of negligence generally will suffice.

D. Private Placements

The most significant remedy to recover damages for misleading or inadequate disclosure in private placements is Rule 10b-5. Rule 10b-5 is discussed in Chapter 14.

E. Exchange Act Violations

As under the Securities Act, any person who violates any provision of the Exchange Act may be liable to the SEC for the greater of disgorgement of profits or penalties ranging from up to \$100,000 for individuals to \$500,000 for entities, for each violation. Additionally, Rule 10b-5 provides a remedy for deficient disclosure in any Exchange Act report or document (e.g., Form 10-K, Form 20-F). Also, Section 18 of the Exchange Act provides an express right of action for false or misleading statements or omissions in any application, report or document filed under the Exchange Act or its rules, whether filed with the SEC or a national securities exchange. However, Section 18 is rarely used because of the difficulties of establishing a Section 18 claim.

In contrast to the strict liability standards of the Securities Act, a person (including the issuer) who makes a material misstatement or omission in an Exchange Act report may assert as a defense that the person acted in good faith and had no knowledge that the statement or omission was false or misleading. However, if any Exchange Act report is incorporated by reference into a Securities Act registration statement (i.e., if the issuer uses a short form registration statement for a future U.S. public offering), the information in the incorporated report becomes subject to Securities Act liability to the same extent as the rest of the registration statement.

F. Control Persons: Directors and Officers

Both the Exchange Act and the Securities Act provide that every person who “controls” an issuer is liable to the same extent as the issuer for violations of the Securities Act, the Exchange Act and related SEC rules. An issuer’s directors and officers (as well as any shareholder with large holdings) should assume they are persons who “control” the issuer. However, a controlling person will generally not be responsible for the issuer’s violation if the person acts in good faith and does not induce the acts constituting the violation.

Nevertheless, the SEC has stated that, in a public report, directors and officers have affirmative responsibilities to assure the accuracy of a public company’s disclosures. If an officer or director knows or should know that his company’s statements are inadequate or incomplete, he has an obligation to correct that failure. An officer or director may rely upon the company’s procedures for determining what disclosure is required only if he has a reasonable basis for believing that those procedures had resulted in full consideration of those issues.

Directors who know of omitted information should not assume that the issuer’s counsel has considered the adequacy of the disclosure, but should discuss this directly with counsel. If the directors are not reasonably satisfied as to the answers they receive, they should insist that the documents be corrected before they are filed with the SEC.

G. Enforcement

1. Class Actions

Class actions are usually brought when an individual plaintiff’s claimed damages are not large but when the total damages alleged to have been sustained are extremely large. Class actions are civil suits brought by an individual plaintiff or group who seek to represent the interests of a much larger group of similarly situated parties (the “class”). A typical example would be a class action on behalf of shareholders who purchased stock on the basis of allegedly misleading information published in a company report filed with the SEC.

2. SEC

The SEC has wide power to investigate, pursue and punish violations of the federal securities laws. The SEC has authority to enforce the regulatory laws by bringing suit in federal court for injunctive relief (i.e., a court order compelling or prohibiting specified conduct). The SEC may seek to enjoin a person from acting as an officer or director of a public company. The SEC may initiate administrative proceedings without court action to order a person to “cease and desist” immediately a violation of the major U.S. securities laws. The SEC may also bring an action in federal court to compel civil penalties for violations of any federal securities law or any cease-and-desist order. For violations involving fraud or reckless disregard of regulatory requirements resulting in substantial loss to others, the penalties are the greater of: (a) \$100,000 for individuals or \$500,000 for corporations, or (b) the gross amount of the pecuniary gain to the defendant. The SEC may also seek disgorgement of profits arising from the defendant’s violation.

3. Criminal Enforcement

Willful violation of the U.S. securities laws may give rise to prosecution by the Department of Justice. The Securities Act provides for fines up to \$10,000 per violation and the Exchange Act provides for fines up to \$5,000,000 for natural persons and \$25,000,000 for entities. Alternatively, fines may be fixed at the greater of twice the profits gained by the defendant or twice the loss inflicted on the victim if that amount is greater than the statute would otherwise provide.⁹⁸ The Department of Justice may also seek imprisonment of up to 5 years for violations of the Securities Act and imprisonment of up to 20 years for violations of the Exchange Act.

The same conduct that violates the U.S. securities laws may also violate the two general U.S. anti-fraud statutes, the mail and wire fraud statutes. To be convicted under the mail or wire fraud statutes, the defendant must have acted to defraud intentionally or with reckless indifference to the truth. A mail or wire fraud conviction can result in fines of up to \$250,000 for an individual, \$500,000 for an entity, or twice the profits gained or loss inflicted by the violation, as well as up to 20 years in prison.⁹⁹

⁹⁸ 18 U.S.C. § 3571(d).

⁹⁹ 18 U.S.C. §§ 1341, 1343, 3571.

**GOING PUBLIC:
A PRACTICAL GUIDE**

**I
Introduction**

Companies that seek to expand their businesses require capital and must compete for available capital. Within the capital raising process, the initial public offering (“IPO”) is one method of obtaining capital. It is a complex, difficult, time consuming and expensive transaction, all of which is aggravated without knowledgeable management and a team of knowledgeable advisers. The company’s team of advisers:

- (a) help management obtain possible financing;
- (b) help management evaluate available alternative financings including an IPO;
- (c) guide management through the financing or public offering; and
- (d) work cooperatively together to complete the financing or public offering quickly and efficiently.

Although timing can be important and it is definitely easier to go public in an active IPO market with relatively high valuations, good companies can go public even in a difficult IPO market.

**II
Deciding Whether to Go Public:
Advantages and Disadvantages of Going Public**

For a company seeking financing, there are numerous advantages to going public. Firstly, equity is cheap, i.e., when a company sells securities in a public offering, it obtains funds for growth that, unlike debt, do not have to be repaid. Similarly, stockholders who sell securities in a public offering increase their personal net worth. Secondly, a public offering results in the creation of a market for trading the company’s securities. An aftermarket (also called a “trading market”) creates liquidity which enables stockholders to sell their shares later, over time, and enhances the attractiveness of the company’s securities and increases the range of future financing alternatives available to the company. An aftermarket facilitates later public offerings and private placements and enables the company to acquire other businesses using its stock rather than all cash. It also creates incentives for employees through their participation in stock option or stock purchase plans which can help the company attract and keep good employees. Many people believe that ownership in a public company offers greater prestige than ownership in a private company, and frequently it fulfills management’s personal goals, all of which results in a feeling of personal success and achievement.

Going public also brings certain obligations which should be carefully considered by management before they undertake an IPO. When a company goes public, it moves from relative privacy to a fishbowl. A public company must disclose and disseminate information that

may otherwise be kept confidential in a privately held company, such as financial statements and information concerning material contracts. Management may lose some flexibility when the company does go public. For example, there are practical limitations on various matters such as salaries, fringe benefits and employing relatives on the company payroll. Business opportunities that formerly may have been personally exploited by the company's former owners must now be offered to the company first. The ability to act quickly may be diminished for significant transactions which require the approval of outside directors or shareholders. Management almost always becomes preoccupied with the company's stock price, trying to keep the stock price up in the face of quarterly pressure for financial results and the short term effect of business decisions on the price of the stock. Expenses increase once a company becomes public. For example, there are increased legal, accounting, transfer agent and, sometimes, public relations fees. Management must also devote time to shareholder relations, public disclosures and dealing with shareholders which can sometimes be unpleasant. An IPO may sometimes lay the groundwork for a former owner later losing control of the company, usually at the insistence of strong professional investors such as venture capitalists who acquired their interest in the company before it became public in a pre-public financing. Lastly, there are legal restrictions on shareholders selling their stock.

The best reason to go public is that the company has reached a stage in its development for which it needs funds to grow, such as modernization, expansion or product development, and applying the funds to that purpose will result in shareholders receiving a high return for their investment.

III

Evaluating Your Company's Ability To Go Public

To evaluate your company's ability to go public, try thinking like an underwriter. After closely examining you and your company, an underwriter will analyze the company and consider the factors set forth below (in rough order of importance), to determine whether he would take your company public. These factors will also affect the underwriter's valuation of the company and the price of its stock:

1. Management. The single most important factor to an underwriter is management. At the outset, management must be able to do two things (among others): (1) describe the company's business simply and concisely, preferably in one sentence; and (2) explain to a prospective underwriter why it would be wise to invest in the company. An underwriter will try to evaluate management's ability, as well as its depth, maturity, commitment, experience, integrity and articulateness. The underwriter will consider whether management invested its own money in the company, whether management will fight every day to make the company a success for the shareholders and management's prior history and background, particularly whether they have any unfavorable matters in their past.

2. Financial performance. The underwriter will evaluate the company's sales (the amount and trend of sales of the company compared with others in the industry), earnings (the source and stability of company earnings as well as future earnings), working capital, cash flow (the adequacy of cash flow for the company's current and future needs) and generally compare the company's financial performance with others in the industry.

3. Potential growth of company. Usually, the greater the company's potential for growth the more attractive the company is to an underwriter. A "good story" may influence an underwriter to overlook some unattractive aspects of a company. However, the less potential for growth the underwriter sees, the greater historical earnings he will usually require.

4. Market. The underwriter will try to ascertain the company's position within its market, the size of that market, if there are entry barriers and the size and character of the future market (over the next 2-4 years).

5. Stability of business. The underwriter will also investigate whether the company depends on one customer or supplier and whether the product is mature.

Some other factors an underwriter will consider are:

6. Alternative sources of financing available to the company;
7. Shareholders' need for liquidity;
8. General market conditions; and
9. Availability of required financial statements.

The ideal characteristics which make a company attractive to an underwriter are:

- (a) an experienced management team with a history of past success and significant ownership interest in the company;
- (b) a company with a history of earnings, an opportunity for future growth and a logical plan for achieving that growth; and
- (c) practical management willing to accept a fairly priced offering with potential to investors for future price appreciation.

IV Selecting The Right Underwriter

Once management decides to finance the company through a public offering, they must find an appropriate underwriter. There are many underwriters and they vary widely in prestige, size, financial strength, ability to provide other services, experience in specific industries, interest in conducting IPOs, requirements for an IPO and size of offerings handled. It is important to be realistic about your company because the company's characteristics determine the range of appropriate underwriters. Some important factors to keep firmly in mind when searching for appropriate underwriters are your company's size, financial performance and industry.

When searching for an appropriate underwriter, also keep in mind the services an investment banker or underwriter provides. Sometimes, management has unrealistic expectations of what services an underwriter can and will provide. Firstly, the managing underwriter provides basic advice about the offering process and the structure of the offering.

Other advice he provides usually includes such things as how to present yourself to institutional investors. Secondly, the underwriter markets the company's securities. He does this by organizing the underwriting syndicate and selling group and managing the offering. As part of this process the underwriter also develops a strategy to help educate the market about the company, its business, prospects and valuation. Thirdly, the underwriter provides post offering support or "sponsorship" to the company. This means making a market in the company's securities for NASDAQ listed companies, preparing research reports on the company and providing general advice to management about such matters as how to keep the markets informed and how to stimulate more comprehensive coverage from the rest of Wall Street.

The characteristics of your company will affect your choice of underwriter. For smaller companies, the goal may be to get any underwriter, while larger or more established or more attractive companies may be able to interview a few firms and choose among them. If you have a choice of underwriters, the golden rule is to choose the best underwriter you can get - but not so large or prestigious that he will not properly service your company. You want an underwriter who will give great attention to your offering. You should be an important client to your underwriter. Therefore, a company making a relatively smaller offering may be better served by a smaller firm or strong regional firm rather than a large national firm.

When choosing an underwriter, you should consider the following characteristics of those prospective underwriters available to you:

1. Reputation.
2. Ability to sell the offering and to whom. This includes the underwriter's:
 - (a) ability to assemble a strong underwriting group,
 - (b) access to retail and institutional customers, and
 - (c) international distribution, if it is important in your industry.
3. Record of successful deals. This is particularly important for smaller underwriters.
4. Aftermarket performance. Determine how the shares of the various companies the underwriter took public are performing in the trading market after the offering.
5. Industry expertise and experience. An underwriter with expertise and experience in your company's industry may better evaluate your company and may be more likely to take it public, may provide a better valuation and may attract other firms who rely on that expertise when participating in the offering, thereby providing greater distribution for the company's securities.
6. Sponsorship. It is important to determine what services the underwriter will provide after the offering is completed such as:
 - (a) market making.

(b) research. Many larger firms will not take a company public unless their research department has an analyst following the company. Determine whether the underwriter will provide research reports on your company.

(c) financial advisory services. Does the underwriter have other capabilities that may help you, i.e., mergers, acquisitions and private placement capabilities.

7. Valuation.

When choosing an underwriter, price should not be the sole determining factor. Do not be too quick to choose the underwriter offering you the highest valuation. Remember, the underwriter is competing for your business and the competition among underwriters can be fierce. Underwriters may be tempted to offer an unrealistically high valuation to obtain your business only to cut it back to the proper price on the eve of the offering when it is too late for you to change underwriters. Question each underwriter and determine how each one arrived at his valuation, then choose among the underwriters that offer the right price.

V Structuring the Offering

Once the company has decided to go public and selected an underwriter, the company and the underwriter negotiate the structure of the offering.

There are two basic types of underwritings, the firm commitment underwriting and the best efforts underwriting. The firm commitment underwriting is the stronger of the two. In a firm commitment underwriting, the underwriter agrees that it will purchase the shares offered by the company and resell them to the public. Once the underwriting agreement is signed, the underwriter is committed to buy the shares regardless of whether it can resell the shares to the public. Since a firm commitment underwriting provides greater assurance of raising funds than a best efforts underwriting, it is more frequently used.

In a best efforts underwriting, the underwriter makes no commitment to purchase the company's securities; the underwriter merely agrees to use its "best efforts" to try to sell the shares offered by the company on a commission basis. To the extent purchasers are not found, the securities are not sold. Some best efforts underwritings will provide that no shares will be sold unless buyers can be found for some minimum percentage of the total offering (e.g., 50% "mini-maxi") or all of the offering ("all or none"). Best efforts offerings usually provide that customer funds will be deposited in an escrow account until the minimum is reached and closing occurs, which can take a relatively long time and is not certain. Therefore, it is frequently difficult for an underwriter of a best efforts offering to attract other firms to participate in a syndicate to market the offering which increases the risk of the underwriter being unable to complete the offering.

The next important issue when structuring an offering is the size of the offering. If the offering is too small, it may be uneconomical given the expense involved. Under the best of circumstances, the offering should be large enough to support a strong, active aftermarket. The number of shares sold to the public (the "float") should be large enough to have a broad distribution, preferably national.

The size of the offering, the number of shares and the price per share of the offering are all interrelated and are based on the valuation of the company determined by the underwriter. The actual number of shares to be offered and the price per share depend on the underwriter's market. Many larger underwriters prefer a share price in the teens, i.e., \$15-\$17 range, so that the offering will be attractive to both institutional and retail investors, while smaller underwriters will price the company's shares lower, frequently in the single digits.

Although most offerings usually are underwritings of common stock, the more speculative offerings frequently include common stock and warrants to purchase additional common stock.

Secondary offerings are offerings of securities by shareholders as compared to securities offered by the company. Secondary offerings are usually disfavored by underwriters and investors because: (a) the funds raised go to the selling shareholders and are not used to build the company, and (b) there is a perception that the shareholders are bailing out of the company at its highest valuation. Therefore, investors believe the securities they purchase will not appreciate further. Investors want to be sure that management believes in the company and that the shareholders will make money with management. Nonetheless, underwriters will do a secondary offering depending on: (a) need of the company for funds, (b) earnings per share of the company, (c) size of offering, and (d) avoidance of the appearance of bail out by insiders. Occasionally, particularly when a prospective offering is otherwise too small, the underwriter may encourage a secondary offering (sales of stock by shareholders) as a way to increase the size of the offering, i.e., the float.

VI

Preparing for the Offering

Timetable and checklist. Once the structure and general terms of the offering have been agreed upon, a detailed timetable and checklist of responsibilities is usually prepared and agreed upon by the working group. An example of a timetable is included in this appendix. Counsel generally aims for a first filing of the registration statement within 4-8 weeks of the "letter of intent" (which is discussed in Chapter 3).

Corporate cleanup. Preparing the company for an offering, also called "corporate cleanup," greatly affects the cost and timing of the offering and is something management should want completed before the underwriter commences his "due diligence" investigation of the company (discussed in Chapter 3). The corporate cleanup includes examining the company's books, records and material contracts to make sure that everything is in order. Beyond that, counsel will check that everything necessary for the offering is in place, such as making sure that company stock has been issued correctly, preparing any recapitalizations, stock splits or increases in authorized shares which may be necessary for the offering and any other matters which have to be accomplished or rectified before the offering.

Accounting issues. During this preparatory phase, management also concentrates on accounting issues such as the independence of the company's accountants, availability of required audited financial statements and unaudited interim statements. The preparation of financial statements may greatly affect the timing of the filing of the company's registration

statement with the Securities and Exchange Commission (“SEC”), since no filing can be made until the required financial statements have been prepared. Accounting issues which may arise are the need for separate or pro forma financial statements for recently acquired companies, the proper reporting method for affiliated entities, any auditor letters reflecting material weaknesses in internal control over financial reporting, related party transactions, stock issuances to employees and segment data and, for foreign private issuers, reconciliation of the financial statements to U.S. generally accepted accounting principles (“U.S. GAAP”) where the financial statements are not prepared under U.S. GAAP or International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

Other matters. Around this time management usually also selects its printer, registrar and transfer agent, and bank note company (which prints the stock certificates).

VII

The Registration Process

Under the Securities Act of 1933 (“Securities Act”), the underwriter cannot begin selling the company’s securities until they have been registered with the SEC. Furthermore, the Securities Act regulates any offers the underwriter may intend to make. Before an underwriter can begin selling a company’s securities, the proposed underwriting must clear three hurdles:

1. registration with the SEC;
2. no objection by the Financial Industry Regulatory Authority (“FINRA”); and
3. exemption from the “blue sky” laws or qualification with the appropriate blue sky authorities (i.e., with the securities administrator of each state in which the offering will be sold).

The rules, regulations and requirements of each of these three affects the structure and timing of the offering and are discussed in Chapter 3.

VIII

Costs of Going Public

The costs of going public can be quite high and are a larger percentage of the offering for smaller offerings than for larger offerings.

Generally underwriter’s commissions range from 6-7% for larger offerings and up to 15% for smaller offerings (when including expense allowances and other items given the underwriter).

The other costs of the offering vary widely depending on numerous factors such as the size of the offering, complexity of the disclosure for the company and its operations, number of amendments, extent and difficulty of the corporate cleanup and SEC comments, among others. The following fees can be expected: SEC and FINRA filing fees, blue sky filing fees, legal fees, accounting fees, and printing, transfer agent and miscellaneous other expenses.

IX Listing Considerations

Requirements for listing on an exchange (including NASDAQ) are important because: (a) listing requirements may affect the structure of the offering, (b) which market you choose affects the aftermarket in the company's securities, and (c) management and shareholders both want the most liquid aftermarket possible. Even smaller companies and their underwriters try to arrange for the company to at least meet the minimum requirements for listing on NASDAQ and avoid being traded on the "Pink Sheets."

X Obligations Once the Company is Public

Once a company goes public, the Securities Exchange Act of 1934 ("Exchange Act") imposes various obligations as do the exchanges (including NASDAQ). Generally, the purpose of these obligations is to maintain fair and informed markets. However, this results in financial and other important information becoming publicly available.

Generally, the obligations imposed on public companies are described in Chapter 9.

XI Conclusion

The process of becoming a public company is a major development in the life of any company. It is a complex, difficult and expensive transaction which should not be undertaken without a careful evaluation of its consequences to the company. If management decides to proceed with a public offering, it should assemble a knowledgeable team of professionals. And, planning for a public offering should begin early. Management that prepares properly and diligently for a public offering can exert greater control over the process and make it more successful.

IPO TIMETABLE

4-8 Weeks	Organizational Meeting Document Drafting and Due Diligence
4-5 Weeks	Filing of Registration Statement SEC Comment Period
3-4 Weeks	Distribution of Preliminary Prospectus (“Red Herring”) Marketing and Road Show
1 Week	Printing and Execution of Underwriting Agreement Selling Completion of Closing Documents Closing
<hr/> Total: 12-18 Weeks	

NYSE Listing Standards

U.S. INITIAL LISTING STANDARDS

Domestic listing requirements call for minimum distribution of a company's shares within the United States as well as minimum financial criteria. Distribution of shares can be attained through U.S. public offerings, acquisitions made in the United States, or by other similar means. Note that there are alternatives to the round-lot holders and pre-tax earnings standards.

When considering a listing application from a company organized under the laws of Canada, Mexico or the United States ("North America"), the NYSE will include all North American holders and North American trading volume in applying the minimum stockholder and trading volume requirements detailed below. For securities that trade in the form of American Depositary Receipts ("ADRs"), volume in the ordinary shares will be adjusted to be on an ADR-equivalent basis.

In addition to meeting the minimum numerical standards listed below, there are other factors the NYSE will consider. The company must be a going concern or be the successor to a going concern.

The NYSE has broad discretion regarding the listing of a company and may deny listing or apply additional or more stringent criteria based on any event, condition or circumstance that makes the listing of the company inadvisable or unwarranted in the opinion of the NYSE. Such determination can be made even if the company meets the quantitative standards set forth below.

Minimum Quantitative Standards: Distribution and Size Criteria

Round-lot Holders (number of holders of a unit of trading – generally 100 shares) ¹	400 U.S.
or ² :	
Total Shareholders ¹	2,200
together with:	
Average Monthly Trading Volume (for the most recent six months)	100,000 shares
or:	
Total Shareholders ¹	500
together with:	
Average Monthly Trading Volume (for the most recent 12 months)	1,000,000 shares

¹ The number of beneficial holders of stock held in "street name" will be considered in addition to the holders of record. The NYSE will make any necessary check of such holdings that are in the name of NYSE member organizations.

² Companies listing in connection with an IPO, affiliated companies and companies listing upon emergence from bankruptcy must have 400 U.S. round-lot holders. The alternative tests based upon the total number of shareholders and average monthly trading volume are unavailable for these companies. The alternative tests are available for companies listing in connection with a transfer or quotation.

Public Shares ³	1,100,000 outstanding
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Continued on Next Page

Market Value of Public Shares^{3,4}:

IPOs, Spin-offs, Affiliated Companies and Initial Firm Commitment Underwritten Public Offerings ⁵	\$40 million
All Other Listings ⁶	\$100 million

³ Shares held by directors, officers or their immediate families and other concentrated holdings of 10% or more are excluded in calculating the number of public shares. For IPOs and Initial Firm Commitment Underwritten Public Offerings (both as defined below), the NYSE will rely on a written commitment from the underwriter to represent the anticipated value of the company's offering in order to determine a company's compliance with this listing standard. Similarly, for spin-offs, the NYSE will rely on a representation from the parent company's investment banker (or other financial adviser) in order to estimate the market value based upon the as disclosed distribution ratio.

⁴ If a company either has a significant concentration of stock or changing market forces have adversely impacted the public market value of a company that otherwise would qualify for a NYSE listing, such that its public market value is no more than 10% below the minimum, the NYSE will generally consider stockholders' equity of \$40 million or \$100 million, as applicable, as an alternate measure of size.

⁵ For this listing standard, an "IPO" is an offering by an issuer that, immediately before its original listing, does not have a class of common stock registered under the Exchange Act. An IPO includes a "carve-out," which is defined for this listing standard as the initial offering of an equity security to the public by a publicly traded company for an underlying interest in its existing business (which may be a subsidiary, division or business unit). For this listing standard, a company is listing in connection with its "Initial Firm Commitment Underwritten Public Offering" if: (i) the company has a class of common stock registered under the Exchange Act, (ii) the common stock has never been listed on a national securities exchange in the period since the commencement of its current registration under the Exchange Act, and (iii) the company is listing in connection with a firm commitment underwritten public offering that is its first firm commitment underwritten public offering of its common stock since the registration of its common stock under the Exchange Act.

A company listing in connection with its Initial Firm Commitment Underwritten Public Offering will generally not have a large public float at the time of initial listing, as there will not have been any prior transaction that led to a significant distribution event and, in the absence of a listing, the company will not have had a liquid trading market. The NYSE believes that these companies are more similar to companies listing in connection with an IPO than to companies transferring from another exchange. As with companies listing in connection with an IPO, these companies are undertaking their first major public distribution of their stock and will have their first truly liquid trading market after listing. As such, the NYSE believes that there is a reasonable basis for concluding that the public float of these companies will increase over time in the same way as is the case for a company after its IPO. Consequently, the NYSE believes it is generally appropriate to subject companies listing in connection with an Initial Firm Commitment Underwritten Public Offering to the same public float requirement as companies listing in connection with an IPO (i.e., \$40 million). Notwithstanding the fact that a company is listing in connection with its Initial Firm Commitment Underwritten Public Offering, the NYSE will apply the \$100 million public float requirement if there is significant trading volume in the company's securities in the over-the-counter market before listing. Additionally, the NYSE will generally apply the \$100 million public float requirement if the company has previously registered on one or more Securities Act registration statements the sale of significant numbers of shares of the class that the company proposes to list (either in direct placements or in best efforts underwritings), unless there is evidence that subsequent trading has been very limited. This is because, in these cases, the company is more similar to a company trading on a national securities exchange than to the closely-held companies with illiquid stocks for which the Initial Firm Commitment Underwritten Public Offering provision was adopted.

⁶ Generally, the NYSE expects to list companies in connection with a firm commitment underwritten IPO, upon transfer from another market, or under a spin-off. However, the NYSE recognizes that some companies that have not previously had their common equity securities registered under the Exchange Act, but that have sold common equity securities in a private placement, may wish to list their common equity securities on the NYSE at

Minimum Quantitative Standards: Financial Criteria

Earnings

Aggregate pre-tax earnings⁷ over the last three fiscal years \$10 million

Minimum in each of the two most recent fiscal years (must be positive amount in all three years) \$2 million

or:

Aggregate pre-tax earnings⁷ over the last three fiscal years \$12 million

Minimum in the most recent fiscal year \$5 million

Minimum in the next most recent fiscal year \$2 million

Or:

Valuation/Revenue with Cash Flow

Global Market Capitalization⁸ \$500 million

the time of effectiveness of a registration statement filed solely for the purpose of allowing existing shareholders to sell their shares. Consequently, the NYSE will, on a case by case basis, exercise discretion to list companies whose stock is not previously registered under the Exchange Act, where such a company is listing without a related underwritten offering upon effectiveness of a registration statement registering only the resale of shares sold by the company in earlier private placements. In exercising this discretion, the NYSE will determine that such company has met the \$100 million aggregate market value of public shares requirement based on a combination of both: (i) an independent third-party valuation (a “Valuation”) of the company, and (ii) the most recent trading price for the company’s common stock in a trading system for unregistered securities operated by a national securities exchange or a registered broker-dealer (a “Private Placement Market”). The NYSE will attribute a market value of public shares to the company equal to the lesser of: (i) the value calculable based on the Valuation, and (ii) the value calculable based on the most recent trading price in a Private Placement Market. Any Valuation used for this purpose must be provided by an entity that has significant experience and demonstrable competence in providing such valuations. The Valuation must be of a recent date as of the time of the approval of the company for listing and the evaluator must have considered, among other factors, the annual financial statements required to be included in the registration statement, along with financial statements for any completed fiscal quarters subsequent to the end of the last year of audited financials included in the registration statement. The NYSE will consider any market factors or factors particular to the listing applicant that would cause concern that the value of the company had diminished since the date of the Valuation and will continue to monitor the company and the appropriateness of relying on the Valuation up to the time of listing. In particular, the NYSE will examine the trading price trends for the stock in the Private Placement Market over a period of several months before listing and will only rely on a Private Placement Market price if it is consistent with a sustained history over that several month period evidencing a market value in excess of the NYSE’s market value requirement. The NYSE may withdraw its approval of the listing at any time before the listing date if it believes that the Valuation no longer accurately reflects the company’s likely market value.

⁷ Pre-tax earnings are adjusted for various items as specified in Section 102.01C of the NYSE Listed Company Manual.

⁸ For companies listing in connection with an IPO or an Initial Firm Commitment Underwritten Public Offering, the company’s underwriter (or, for a spin-off, the parent company’s investment banker or other financial adviser) must provide a written representation that demonstrates the company’s ability to meet the \$500 million global market capitalization requirement based upon the completion of the offering (or distribution).

The NYSE will, on a case by case basis, exercise discretion to list companies whose common stock is not previously registered under the Exchange Act, where such a company is listing without a related underwritten offering upon effectiveness of a registration statement registering only the resale of shares sold by the company in earlier private placements. In such cases, the NYSE will determine that the company has met the global market capitalization value requirement based on a combination of both: (i) an independent third-party valuation (a “Valuation”) of the company, and (ii) the most recent trading price for the company’s common stock in a trading system for unregistered securities operated by a national securities exchange or a registered broker-dealer (a “Private

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Revenues (most recent 12-month period)	\$100 million
Aggregate Operating Cash Flow ⁹ over the last three fiscal years (each year must report a positive amount)	\$25 million
Or:	
Pure Valuation/Revenue	
Global Market Capitalization ¹⁰	\$750 million

Placement Market”). The NYSE will list a company using this approach only if it determines that the company has a global market capitalization of \$600 million. The NYSE will attribute a global market capitalization to the company equal to the lesser of: (i) the value calculable based on the Valuation, and (ii) the value calculable based on the most recent trading price in a Private Placement Market. Any Valuation used for this purpose must be provided by an entity that has significant experience and demonstrable competence in providing such valuations. The Valuation must be of a recent date as of the time of the approval of the company for listing and the evaluator must have considered, among other factors, the annual financial statements required to be included in the registration statement, along with financial statements for any completed fiscal quarters subsequent to the end of the last year of audited financials included in the registration statement. The NYSE will consider any market factors or factors particular to the listing applicant that would cause concern that the value of the company had diminished since the date of the Valuation and will continue to monitor the company and the appropriateness of relying on the Valuation up to the time of listing. In particular, the NYSE will examine the trading price trends for the stock in the Private Placement Market over a period of several months before listing and will only rely on a Private Placement Market price if it is consistent with a sustained history over that several month period evidencing a market value in excess of the NYSE’s market value requirement. The NYSE may withdraw its approval of the listing at any time before the listing date if it believes that the Valuation no longer accurately reflects the company’s likely market value.

⁹ Represents net cash provided by operating activities excluding the changes in working capital or in operating assets and liabilities, as adjusted for various items as specified in Section 102.01C of the NYSE Listed Company Manual.

¹⁰ For companies listing in connection with an IPO or an Initial Firm Commitment Underwritten Public Offering, the company’s underwriter (or, for a spin-off, the parent company’s investment banker or other financial adviser) must provide a written representation that demonstrates the company’s ability to meet the \$750 million global market capitalization requirement based upon the completion of the offering (or distribution). For all other companies, market capitalization valuation will be determined over a three-month average. In considering the suitability for listing of a company under the provision in the immediately preceding sentence, the NYSE will consider whether the company’s business prospects and operating results indicate that the company’s market capitalization value is likely to be sustained or increase over time.

The NYSE will, on a case by case basis, exercise discretion to list companies whose common stock is not previously registered under the Exchange Act, where such a company is listing without a related underwritten offering upon effectiveness of a registration statement registering only the resale of shares sold by the company in earlier private placements. In such cases, the NYSE will determine that the company has met the global market capitalization value requirement based on a combination of both: (i) an independent third-party valuation (a “Valuation”) of the company, and (ii) the most recent trading price for the company’s common stock in a trading system for unregistered securities operated by a national securities exchange or a registered broker-dealer (a “Private Placement Market”). The NYSE will list a company using this approach only if it determines that the company has a global market capitalization of \$900 million. The NYSE will attribute a global market capitalization to the company equal to the lesser of: (i) the value calculable based on the Valuation, and (ii) the value calculable based on the most recent trading price in a Private Placement Market. Any Valuation used for this purpose must be provided by an entity that has significant experience and demonstrable competence in providing such valuations. The Valuation must be of a recent date as of the time of the approval of the company for listing and the evaluator must have considered, among other factors, the annual financial statements required to be included in the registration statement, along with financial statements for any completed fiscal quarters subsequent to the end of the last year of audited financials included in the registration statement. The NYSE will consider any market factors or factors

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Revenues (most recent fiscal year) \$75 million

Or:

Affiliated Company (for new entities with a parent or affiliated company listed on the NYSE). Original distribution requirements as noted; global market capitalization of \$500 million or greater;⁸ company must have at least 12 months of operating history (although it is not required to have been a separate corporate entity for that long); company's parent or affiliated company is a listed company in good standing (as evidenced by written representation from the company or its financial adviser excluding that portion of the balance sheet attributable to the new entity); and company's parent or affiliated company retains control of the entity or is under common control with the entity.¹¹

Or:

Assets and Equity¹²

Global Market Capitalization¹³ \$150 million

particular to the listing applicant that would cause concern that the value of the company had diminished since the date of the Valuation and will continue to monitor the company and the appropriateness of relying on the Valuation up to the time of listing. In particular, the NYSE will examine the trading price trends for the stock in the Private Placement Market over a period of several months before listing and will only rely on a Private Placement Market price if it is consistent with a sustained history over that several month period evidencing a market value in excess of the NYSE's market value requirement. The NYSE may withdraw its approval of the listing at any time before the listing date if it believes that the Valuation no longer accurately reflects the company's likely market value.

¹¹ For the Affiliated Company Test, "control" means having the ability to exercise significant influence over the operating and financial policies of the listing company, and will be presumed to exist where the parent or affiliated company holds 20% or more of the listing company's voting stock directly or indirectly. Other indicia that may be taken into account when determining whether control exists include board representation, participation in policy making processes, material intercompany transactions, interchange of managerial personnel and technological dependency. The Affiliated Company Test is taken from and intended to be consistent with generally accepted accounting principles regarding use of the equity method of accounting for an investment in common stock.

¹² Special purpose acquisition companies ("SPACs") are not permitted to list under the Assets and Equity Test. SPACs will only be listed if they meet the requirements of Section 102.06 of the NYSE Listed Company Manual (discussed below).

¹³ In considering the listing under the Assets and Equity Test of companies transferring from other markets, the NYSE will consider whether the company's business prospects and operating results indicate that the company's market capitalization value is likely to be sustained or increase over time.

For companies listing in connection with an IPO or an Initial Firm Commitment Underwritten Public Offering, the company's underwriter (or, for a spin-off, the parent company's investment banker or other financial adviser) must provide a written representation that demonstrates the company's ability to meet the \$150 million global market capitalization requirement based upon the completion of the offering (or distribution).

The NYSE will, on a case by case basis, exercise discretion to list companies whose common stock is not previously registered under the Exchange Act, where such a company is listing without a related underwritten offering upon effectiveness of a registration statement registering only the resale of shares sold by the company in earlier private placements. In such cases, the NYSE will determine that the company has met the global market capitalization value requirement based on a combination of both: (i) an independent third-party valuation (a "Valuation") of the company, and (ii) the most recent trading price for the company's common stock in a trading system for unregistered securities operated by a national securities exchange or a registered broker-dealer (a "Private Placement Market"). The NYSE will list a company using this approach only if it determines that the company has a global market capitalization of \$180 million. The NYSE will attribute a global market capitalization to the company equal to the lesser of: (i) the value calculable based on the Valuation, and (ii) the value calculable based on the most recent trading price in a Private Placement Market. Any Valuation used for this purpose must be provided

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Total Assets	\$75 million
Stockholders Equity	\$50 million
Or:	
Real Estate Investment Trusts (“REITs”) (with less than three years operating history)	
Stockholders’ Equity ¹⁴	\$60 million
Or:	
Funds and Business Development Companies (“BDCs”)	
Market Value of Public Shares	\$60 million
Or:	
SPACs¹⁵	
Proceeds held in trust upon IPO	90%
Fair Market Value of Acquisitions (% of net assets)	80%
Aggregate Market Value	\$250 million
Market Value of Public Shares ¹⁶	\$200 million

Minimum Quantitative Standards: Stock Price Criteria

Stock Price ¹⁷	\$4
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by an entity that has significant experience and demonstrable competence in providing such valuations. The Valuation must be of a recent date as of the time of the approval of the company for listing and the evaluator must have considered, among other factors, the annual financial statements required to be included in the registration statement, along with financial statements for any completed fiscal quarters subsequent to the end of the last year of audited financials included in the registration statement. The NYSE will consider any market factors or factors particular to the listing applicant that would cause concern that the value of the company had diminished since the date of the Valuation and will continue to monitor the company and the appropriateness of relying on the Valuation up to the time of listing. In particular, the NYSE will examine the trading price trends for the stock in the Private Placement Market over a period of several months before listing and will only rely on a Private Placement Market price if it is consistent with a sustained history over that several month period evidencing a market value in excess of the NYSE’s market value requirement. The NYSE may withdraw its approval of the listing at any time before the listing date if it believes that the Valuation no longer accurately reflects the company’s likely market value.

¹⁴ For those REITs listing in conjunction with an offering, this requirement must be evidenced by a written commitment from the underwriter (or, for a spin-off or carve-out, from the parent company’s investment banker or other financial adviser) on behalf of the REIT.

¹⁵ The NYSE will consider on a case-by-case basis, the appropriateness for listing of SPACs with no prior operating history that conduct an IPO if the criteria in the text are met.

¹⁶ Shares held by directors, officers or their immediate families and other concentrated holdings of 10% or more are excluded in calculating the number of public shares. For SPACs that list at the time of their IPOs, if necessary, the NYSE will rely on a written commitment from the underwriter to represent the anticipated value of the SPAC’s offering in order to determine a SPAC’s compliance with this listing standard.

¹⁷ A company must have a closing price or, if listing in connection with an IPO or Initial Firm Commitment Underwritten Public Offering, an IPO or Initial Firm Commitment Underwritten Public Offering price per share, of at least \$4 at the time of initial listing.

NYSE Listing Standards

NON-U.S. (“WORLDWIDE”) INITIAL LISTING STANDARDS

Non-U.S. corporations may elect to qualify for listing under either the alternate, worldwide listing standards or the NYSE’s domestic listing criteria. However, an applicant company must meet all of the criteria within the standards under which it seeks to qualify for listing.

CRITERIA	REQUIREMENTS	WORLDWIDE	DOMESTIC May satisfy either A, B, or C:
Distribution and Size	Round-Lot Holders Total Shareholders	5,000	A. 400 U.S. round lot shareholders B. 2,200 total shareholders and 100,000 shares average monthly trading volume (for the most recent six months) C. 500 total shareholders and 1,000,000 shares average monthly trading volume (for the most recent 12 months)
	Public Shares	2.5MM ¹	1.1MM
	Market Value of Public Shares		
	IPOs, Carve-outs, Spin-offs and Initial Firm Commitment Underwritten Public Offerings	\$100MM ²	\$40MM
	Affiliated Companies	\$60MM	\$40MM
	All Other Listings	\$100MM ³	\$100MM

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¹ Shares held by directors, officers or their immediate families and other concentrated holdings of 10% or more are excluded in calculating the number of public shares.

² If a company either has a significant concentration of stock or changing market forces have adversely impacted the public market value of a company that otherwise would qualify for a NYSE listing, such that its public market value is no more than 10% below \$100 million, the NYSE will generally consider stockholders' equity of \$100 million as an alternate measure of size.

For IPOs and Initial Firm Commitment Underwritten Public Offerings, if necessary, the NYSE will rely on a written commitment from the underwriter to represent the anticipated value of the company's offering in order to determine a company's compliance with this listing standard. Similarly, for spin-offs, the NYSE will rely on a representation from the parent company's investment banker (or other financial adviser) or transfer agent in order to estimate the market value based upon the as disclosed distribution ratio. For this listing standard, an “IPO” includes a spin-off and is an offering by an issuer that, immediately before its original listing, does not have a class of common stock registered under the Exchange Act. An IPO includes a “carve-out,” which is defined for this listing standard as the initial offering of an equity security to the public by a publicly traded company for an underlying interest in its existing business (which may be a subsidiary, division or business unit).

³ If a company either has a significant concentration of stock or changing market forces have adversely impacted the public market value of a company that otherwise would qualify for a NYSE listing, such that its public market value is no more than 10% below \$100 million, the NYSE will generally consider stockholders' equity of \$100 million as an alternate measure of size.

Financial	Earnings		
	Aggregate pre-tax earnings over the last three fiscal years	\$100MM ⁴	\$10MM
	Minimum in each of the two most recent fiscal years	\$25MM	\$2MM (must be positive amount in all three years)
	or:		
	Aggregate pre-tax earnings over the last three fiscal years	N/A	\$12MM
	Minimum in the most recent fiscal year	N/A	\$5MM
	Minimum in the next most recent fiscal year	N/A	\$2MM
	Or:		
	Valuation/Revenue May satisfy either A. or B.		
	A. Valuation/Revenue with Cash Flow		
	Global Market Capitalization	\$500MM ⁵	\$500MM
	Revenues (most recent 12-month period)	\$100MM	\$100MM
	Aggregate Operating Cash Flow over the last three fiscal years	\$100MM ⁶	\$25MM (each year must report a positive amount)
	Minimum Cash Flow in each of the two most recent years	\$25MM	N/A
	B. Pure Valuation/Revenue		
	Global Market Capitalization	\$750MM ⁷	\$750MM
	Revenues (most recent fiscal year)	\$75MM	\$75MM

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⁴ Pre-tax earnings are adjusted for various items as specified in Section 102.01C and Section 103.01B of the NYSE Listed Company Manual.

Reconciliation to U.S. GAAP of the third year back would only be required if the NYSE determines that reconciliation is necessary to demonstrate that the aggregate \$100 million threshold is satisfied.

⁵ For companies listing in connection with an IPO or an Initial Firm Commitment Underwritten Public Offering, the company's underwriter (or, for a spin-off, the parent company's investment banker or other financial adviser) must provide a written representation that demonstrates the company's ability to meet the \$500 million global market capitalization requirement based upon the completion of the offering (or distribution).

⁶ Represents net cash provided by operating activities excluding the changes in working capital or in operating assets and liabilities, as adjusted for various items as specified in Section 102.01C of the NYSE Listed Company Manual.

⁷ For companies listing in connection with an IPO or an Initial Firm Commitment Underwritten Public Offering, the company's underwriter (or, for a spin-off, the parent company's investment banker or other financial adviser) must provide a written representation that demonstrates the company's ability to meet the \$750 million global market capitalization requirement based upon the completion of the offering (or distribution). For all other companies, market capitalization valuation will be determined over a six-month average.

	Or:		
	Affiliated Company (for new entities with a parent or affiliated company listed on the NYSE).		
	Global Market Capitalization	\$500MM ⁸	\$500MM
	<ul style="list-style-type: none"> • Company must have at least 12 months of operating history (although it is not required to have been a separate corporate entity for that long). • Company's parent or affiliated company is a listed company in good standing (as evidenced by written representation from the company or its financial adviser excluding that portion of the balance sheet attributable to the new entity). • Company's parent or affiliated company retains control of the entity or is under common control with the entity. 	<p>Yes</p> <p>Yes</p> <p>Yes⁹</p>	<p>Yes</p> <p>Yes</p> <p>Yes</p>
Price	Stock Price	\$4 ¹⁰	\$4

⁸ For companies listing in connection with an IPO or an Initial Firm Commitment Underwritten Public Offering, the company's underwriter (or, for a spin-off, the parent company's investment banker or other financial adviser) must provide a written representation that demonstrates the company's ability to meet the \$500 million global market capitalization requirement based upon the completion of the offering (or distribution).

⁹ For the Affiliated Company Test, "control" means having the ability to exercise significant influence over the operating and financial policies of the listing company, and will be presumed to exist where the parent or affiliated company holds 20% or more of the listing company's voting stock directly or indirectly. Other indicia that may be taken into account when determining whether control exists include board representation, participation in policy making processes, material intercompany transactions, interchange of managerial personnel and technological dependency. The Affiliated Company Test is taken from and intended to be consistent with generally accepted accounting principles regarding use of the equity method of accounting for an investment in common stock.

¹⁰ A company must have a closing price or, if listing in connection with an IPO or Initial Firm Commitment Underwritten Public Offering, a public offering price per share, of at least \$4 at the time of listing.

NYSE Amex Listing Standards

The NYSE Amex has established certain quantitative and qualitative standards for initial listing of U.S. and foreign companies.

Quantitative Standards

Criteria	Listing Standards			
	Standard 1	Standard 2	Standard 3	Standard 4
Pre-tax income ¹	\$750,000	N/A	N/A	N/A
Market capitalization	N/A	N/A	\$50 million	\$75 million OR At least \$75 million in total assets and \$75 million in total revenues ¹
Market value of public float	\$3 million	\$15 million	\$15 million	\$20 million
Minimum price	\$3	\$3	\$2	\$3
Operating history	N/A	two years	N/A	N/A
Shareholders' equity	\$4 million	\$4 million	\$4 million	N/A
Public shareholders/ Public float (shares) ²	Option 1: 800/500,000 Option 2: 400/1,000,000 Option 3: 400/500,000 ³			

Foreign Applicants

Foreign issuer applicants that do not meet the distribution guidelines outlined above may alternatively qualify with 800 round-lot public shareholders worldwide, one million publicly held shares worldwide and a \$3 million market value of public float worldwide.

Initial Public Offerings

In certain circumstances, the NYSE Amex may approve an issue for listing “subject to official notice of issuance” immediately before effectiveness of the issuer applicant’s IPO. While the NYSE Amex has not adopted special criteria for IPOs, added emphasis is placed on the company’s financial strength, including an objective evaluation of the anticipated value and offering price, and its demonstrated earnings history and/or outlook.

Qualitative Standards

In evaluating listing eligibility, the NYSE Amex also considers qualitative factors such as the nature of a company’s business, market for its products, reputation of its management, historical record and pattern of growth, financial integrity, demonstrated earnings power and future outlook. The NYSE Amex also considers the laws, customs and practices of the applicant’s country of

¹ Required in the latest fiscal year, or two of the three most recent fiscal years.

² Public shareholders and public float do not include shareholders or shares held directly or indirectly by any officer, director, controlling shareholder or other concentrated (i.e., 10% or greater), affiliated or family holdings.

³ Option 3 requires a daily trading volume of 2,000 shares during the six months before listing.

domicile concerning matters such as the election and composition of the board of directors, issuance of quarterly earning statements, shareholder approval requirements and quorum requirements.

Corporate Governance Standards

The NYSE Amex requires listed companies to adhere to its corporate governance standards.

Conflicts of Interest

The NYSE Amex requires a listed company to use its audit committee to conduct an appropriate review of all related party transactions on an ongoing basis. See Section 120 of the NYSE Amex Company Guide.

Independent Directors and Audit Committee

The NYSE Amex has various requirements concerning a company's independent directors and audit committee. Any domestic issuer applying for listing on the NYSE Amex must be prepared to demonstrate compliance with these requirements and ongoing compliance is also required for listed companies. See Section 121 and Part 8 (Corporate Governance Requirements) of the NYSE Amex Company Guide.

Quorum

The NYSE Amex expects that an appropriate quorum of the shares issued and outstanding and entitled to vote will be provided for by the bylaws of companies applying for the original listing of voting securities. A quorum of at least 33-1/3% is recommended. See Section 123 of the NYSE Amex Company Guide.

Shareholder Approval

The NYSE Amex requires listed companies to obtain shareholder approval for certain corporate actions that would result in discounted stock and/or option issuances as well as other potentially dilutive transactions. See Sections 711, 712 and 713 of the NYSE Amex Company Guide.

Voting Rights

Common Stock-See Section 122 of the NYSE Amex Company Guide.

Preferred Stock-See Section 124 of the NYSE Amex Company Guide.

NYSE Arca Listing Standards

NYSE Arca has broader eligibility requirements than the NYSE.

Formerly, NYSE Arca had two listing tiers: Tier I and Tier II. Each tier had its own set of initial listing requirements. Tier I was designed for large capitalization mature companies, and federal securities laws provide that Tier I listed companies are exempt from all state registration requirements, known as "blue sky" laws. As of November 2006, NYSE Arca discontinued listing new issuers and new classes of securities under Tier II, and all new listings will effectively be Tier I.

Initial Listing Standards	
Distribution Minimums	
Public Round-lot Holders	400
Publicly Held Shares	1,100,000
Closing Price per Share	\$5.00 for 90 consecutive trading days
Financial Minimums (based on U.S. GAAP)	
Market Capitalization	\$150 million
Market Value of Publicly Held Shares	\$45 million
Must meet at least two of the following four minimums:	
Total Assets	\$75 million
Revenue (most recent year or two of last three)	\$50 million
Shareholders' Equity	\$50 million
Pre-tax earnings in last fiscal year	Positive

NASDAQ Listing Standards

NASDAQ Global Select Market

Companies must meet all of the criteria under at least one of the four financial standards and the applicable liquidity requirements below for initial listing on the NASDAQ Global Select Market.

FINANCIAL AND QUALITATIVE REQUIREMENTS¹

Requirements	Standard 1 Listing Rules 5315(e) and 5315(f)(3)(A)	Standard 2 Listing Rules 5315(e) and 5315(f)(3)(B)	Standard 3 Listing Rules 5315(e) and 5315(f)(3)(C)	Standard 4 Listing Rules 5315(e) and 5315(f)(3)(D)
Pre-tax earnings ² (income from continuing operations before income taxes)	Aggregate in prior three fiscal years \geq \$11 million and Each of the two most recent fiscal years \geq \$2.2 million and Each of the prior three fiscal years \geq \$0	N/A	N/A	N/A
Cash flows ³	N/A	Aggregate in prior three fiscal years \geq \$27.5 million and Each of the prior three fiscal years \geq \$0	N/A	N/A

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¹ These requirements apply to all companies, other than closed-end management investment companies. A closed-end management investment company, including a business development company, is not required to meet the financial requirements of Listing Rule 5315(f)(3). In lieu of meeting Rule 5315(f)(3), a business development company must have a Market Value of Listed Securities of at least \$80 million. If the common stock of an issuer is included in the NASDAQ Global Select Market, any other security of that same issuer, such as other classes of common or preferred stock, that qualifies for listing on the NASDAQ Global Market will also be included in the NASDAQ Global Select Market. An issuer whose business plan is to complete an IPO and engage in a merger or acquisition with one or more unidentified companies within a specified period of time, as described in IM-5101-2, is not eligible to list on the Nasdaq Global Select Market.

² In calculating income from continuing operations before income taxes for Rule 5315(f)(3)(A), NASDAQ will rely on an issuer's annual financial information as filed with the SEC in the issuer's most recent periodic report and/or registration statement. If an issuer does not have three years of publicly reported financial data, it may qualify under Rule 5315(f)(3)(A) if it has: (i) reported aggregate income from continuing operations before income taxes of at least \$11 million, and (ii) positive income from continuing operations before income taxes in each of the reported fiscal years. A period of less than three months will not be considered a fiscal year, even if reported as a stub period in the issuer's publicly reported financial statements.

³ In calculating cash flows for Rule 5315(f)(3)(B), NASDAQ will rely on the net cash provided by operating activities reported in the statements of cash flows, as filed with the SEC in the issuer's most recent periodic report and/or registration statement, excluding changes in working capital or in operating assets and liabilities. If an issuer does not have three years of publicly reported financial data, it may qualify under Rule 5315(f)(3)(B) if it has: (i) reported aggregate cash flows of at least \$27.5 million, and (ii) positive cash flows in each of the reported fiscal years. A period of less than three months will not be considered a fiscal year, even if reported as a stub period in the issuer's publicly reported financial statements.

Market capitalization ⁴	N/A	Average ≥ \$550 million over prior 12 months	Average ≥ \$850 million over prior 12 months	\$160 million
Revenue	N/A	Previous fiscal year ≥ \$110 million	Previous fiscal year ≥ \$90 million	N/A
Total assets	N/A	N/A	N/A	\$80 million in the most recently completed fiscal year
Stockholders' equity	N/A	N/A	N/A	\$55 million
Bid price ⁵	\$4.00	\$4.00	\$4.00	\$4.00
Market makers ⁶	3 or 4	3 or 4	3 or 4	3 or 4
Corporate governance ⁷	Yes	Yes	Yes	Yes

⁴ For an issuer listing in connection with its IPO, compliance with the market capitalization requirements of Rules 5315(f)(3)(B), (C) and (D) will be based on the company's market capitalization at the time of listing.

⁵ The bid price requirement is not applicable to a company listed on the NASDAQ Global Market that transfers its listing to the NASDAQ Global Select Market.

⁶ A company that also satisfies the requirements of Rule 5405(b)(1) or 5405(b)(2) is required to have three market makers. Otherwise, the company is required to have four market makers. An electronic communications network ("ECN") is not considered a market maker for these rules.

⁷ In addition to the above quantitative requirements, companies must comply with all corporate governance requirements as set forth in the Rule 5600 Series.

LIQUIDITY REQUIREMENTS

Companies must meet all of the criteria in their specific category. The charts below are presented in two separate groups: (i) new company listings, and (ii) closed-end management investment companies.

New Company Listings				
Requirements	Initial Public Offerings and Spin-Off Companies	Seasoned Companies: Currently Trading Common Stock or Equivalents	Affiliated Companies ⁸	Listing Rules
Round lot shareholders or Total shareholders or Total shareholders and Average monthly trading volume over past 12 months ⁹	450 or 2,200	450 or 2,200 or 550 and 1.1 million	450 or 2,200 or 550 and 1.1 million	5315(f)(1)
Publicly held shares ¹⁰	1,250,000	1,250,000	1,250,000	5315(e)(2)
Market value of publicly held shares or Market value of publicly held shares and Stockholders' equity	\$45 million	\$110 million or \$100 million and \$110 million	\$45 million	5315(f)(2)

⁸ “Affiliated Companies” are companies affiliated with another company listed on the NASDAQ Global Select Market. For Rule 5315, a company is “affiliated with” another company if that other company, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control of, the company. For these rules, “control” means having the ability to exercise significant influence. “Ability to exercise significant influence” will be presumed to exist where the parent or affiliated company directly or indirectly owns 20% or more of the other company’s voting securities, and also can be indicated by representation on the board of directors, participation in policy making processes, material intercompany transactions, interchange of managerial personnel or technological dependency.

⁹ Round lot and total shareholders include both beneficial holders and holders of record.

¹⁰ “Publicly held shares” is defined as total shares outstanding, less any shares held directly or indirectly by officers, directors or any person who is the beneficial owner of more than 10% of the total shares outstanding of the company.

Closed-End Management Investment Companies				
Requirements	Fund Groups	Closed-End Funds Not Part of a Group	Business Development Companies	Listing Rules
Round lot shareholders or Total shareholders or Total shareholders and Average monthly trading volume over past twelve months	450 or 2,200 or 550 and 1.1 million	450 or 2,200 or 550 and 1.1 million	450 or 2,200 or 550 and 1.1 million	5315(f)(1)
Publicly held shares	1,250,000	1,250,000	1,250,000	5315(e)(2)
Market value of publicly held shares for each fund and Total MVPHS for fund group and Average MVPHS for all funds in group	\$35 million and \$220 million and \$50 million	\$70 million	\$70 million	5315(c) 5315(f)(2)(D)
Market value of listed securities	N/A	N/A	\$80 million	5315(d)

NASDAQ Global Market

A company must meet all of the criteria under at least one of the four standards below for initial listing on the NASDAQ Global Market.

NASDAQ Global Market Initial Listing Requirements¹

Requirements	Initial Listing			
	Income Standard Listing Rules 5405(a) and 5405(b)(1)	Equity Standard Listing Rules 5405(a) and 5405(b)(2)	Market Value Standard Listing Rules 5405(a) and 5405(b)(3) ²	Total Assets/Total Revenue Standard Listing Rules 5405(a) and 5405(b)(4)
Stockholders' equity	\$15 million	\$30 million	N/A	N/A
Market value of listed securities ³	N/A	N/A	\$75 million	N/A
Total assets and Total revenue (in latest fiscal year or in two of last three fiscal years)	N/A	N/A	N/A	\$75 million and \$75 million
Income from continuing operations before income taxes (in latest fiscal year or in two of last three fiscal years)	\$1 million	N/A	N/A	N/A
Publicly held shares ⁴	1.1 million	1.1 million	1.1 million	1.1 million
Market value of publicly held shares	\$8 million	\$18 million	\$20 million	\$20 million
Bid price	\$4	\$4	\$4 ²	\$4
Shareholders (round lot holders) ⁵	400	400	400	400
Market makers ⁶	3	3	4	4
Operating history	N/A	2 years	N/A	N/A
Corporate governance	Yes	Yes	Yes	Yes

¹ Companies must meet the bid price, publicly held shares and round lot holders requirements as set forth in Rule 5405(a) and at least one of the Standards in Rule 5405(b).

² Seasoned companies (those companies already listed or quoted on another marketplace) qualifying only under the Market Value Standard must meet the market value of listed securities and bid price requirements for 90 consecutive trading days before applying for listing.

³ The term "listed securities" is defined as "securities listed on NASDAQ or another national securities exchange."

⁴ "Publicly held shares" is defined as total shares outstanding, less any shares held directly or indirectly by officers, directors or any person who is the beneficial owner of more than 10% of the total shares outstanding of the company.

⁵ "Round lot holders" are shareholders of 100 shares or more. The number of beneficial holders is considered in addition to holders of record.

⁶ An electronic communications network ("ECN") is not considered a market maker for these rules.

NASDAQ Capital Market

A company must meet all of the criteria under at least one of the three standards below for initial listing on the NASDAQ Capital Market.

NASDAQ Capital Market Initial Listing Requirements¹

Requirements	Equity Standard Listing Rules 5505(a) and 5505(b)(1)	Market Value of Listed Securities Standard Listing Rules 5505(a) and 5505(b)(2) ²	Net Income Standard Listing Rules 5505(a) and 5505(b)(3)
Stockholders' equity	\$5 million	\$4 million	\$4 million
Market value of publicly held shares	\$15 million	\$15 million	\$5 million
Operating history	2 years	N/A	N/A
Market value of listed securities ³	N/A	\$50 million	N/A
Net income from continuing operations (in the latest fiscal year or in two of the last three fiscal years)	N/A	N/A	\$750,000
Publicly held shares ⁴	1 million	1 million	1 million
Bid price	\$4	\$4	\$4
Shareholders (round lot holders) ⁵	300	300	300
Market makers ⁶	3	3	3
Corporate governance	Yes	Yes	Yes

¹ Companies must meet the bid price, publicly held shares, round lot holders and market makers requirements as set forth in Rule 5505(a) and at least one of the Standards in Rule 5505(b).

² Seasoned companies (those companies already listed or quoted on another marketplace) qualifying only under the Market Value of Listed Securities Standard must meet the market value of listed securities and bid price requirements for 90 consecutive trading days before applying for listing.

³ The term "listed securities" is defined as "securities listed on NASDAQ or another national securities exchange."

⁴ "Publicly held shares" is defined as total shares outstanding, less any shares held directly or indirectly by officers, directors or any person who is the beneficial owner of more than 10% of the total shares outstanding of the company. In the case of ADRs, at least 400,000 must be issued.

⁵ "Round lot holders" are shareholders of 100 shares or more. The number of beneficial holders is considered in addition to holders of record.

⁶ An electronic communications network ("ECN") is not considered a market maker for these rules.

Over the Counter Bulletin Board (“OTCBB”) Eligibility Requirements

Because the OTCBB is a quotation service for FINRA market makers, not an issuer listing service or securities market, there are no listing requirements that must be met by an OTCBB issuer. Accordingly, there are no financial requirements and there is no minimum bid price requirement. While the OTCBB does not have any listing requirements per se, for a security to be eligible for quotation on the OTCBB, the security must be registered with the SEC or other federal regulatory authority that has proper jurisdiction and the issuer of the security must remain current in its filings with the SEC or other applicable regulatory authority.¹ Market makers must not begin quotation of a security on the OTCBB unless the issuer of the security is current in its filings with the SEC or other applicable regulatory authority.²

¹ Domestic issues quoted on the OTCBB are limited to the following securities: (a) securities of issuers that make current filings under Section 13 or 15(d) of the Exchange Act; (b) securities of depository institutions that are not required to make filings under the Exchange Act, but file publicly available reports with their appropriate regulatory authorities; (c) securities of registered closed-end investment companies; and (d) securities of insurance companies that are exempt from Exchange Act registration under Section 12(g)(2)(G) of that Act. Foreign issues and ADRs must be registered with the SEC under Section 12 of the Exchange Act. See FINRA Rule 6530 (OTCBB-Eligible Securities).

² See FINRA Rule 6540 (Requirements Applicable to Market Makers).

SARBANES-OXLEY COMPLIANCE CHECKLIST

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
1. Section 302 Civil Certification by CEO and CFO.	Yes. Must include in Forms 20-F and 40-F, but <u>not</u> Form 6-K.
2. Section 906 Criminal Certification by CEO and CFO.	Yes. Must include in Forms 20-F and 40-F, but <u>not</u> Form 6-K.
3. Accelerated 2-business day filing for Form 4 by corporate insiders.	No.
4. Ban on personal loans or other extensions of credit to directors and executive officers. SOX's prohibition on personal loans does not apply to any loan made (or maintained) by a Federal Deposit Insurance Corporation (FDIC)-insured bank or savings association if the loan is subject to the insider lending restrictions of Section 22(h) of the Federal Reserve Act.	Yes. This exemption does not apply to non-U.S. banks because they are not FDIC-insured. However, the SEC has adopted Rule 13k-1 under the Exchange Act, which remedies this disparate treatment of foreign banks by exempting from SOX's insider lending prohibition those foreign banks that meet specified criteria similar to those that qualify U.S. banks for the statutory exemption.
5. Material correcting adjustments identified by auditing firm must be reflected in financial reports.¹	Yes.
6. Forfeiture by CEO and CFO of bonus and equity compensation if financials restated as a result of misconduct.²	Yes. However, applying this provision to non-U.S. issuers may be difficult if any required repayment would violate the employment laws of a non-U.S. jurisdiction.

¹ Under Section 401(a) of SOX, each financial report that contains financial statements, and that is required to be prepared in accordance with (or reconciled to) U.S. GAAP and filed with the SEC, must reflect all material correcting adjustments identified by a registered public accounting firm in accordance with U.S. GAAP and SEC rules. (Registered investment companies are exempt from Section 401(a) of SOX.)

² Under Section 304 of SOX, if an issuer must restate its financial statements because of misconduct that results in its material non-compliance with any financial reporting requirement under the federal securities laws, the issuer's CEO and CFO must reimburse the issuer for: (a) any bonus or other incentive-based or equity-based compensation received during the 12 months following the first public issuance or filing with the SEC (whichever is earlier) of the financial document embodying the financial reporting requirement, and (b) any profits realized from the sale of the issuer's securities during those 12 months.

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
<p>7. No retaliation against employees for whistleblowing.³</p>	<p>Yes. However, in June 2006, in <i>Carnero v. Boston Scientific Corp.</i>, the U.S. Supreme Court declined to consider whether this provision of SOX (i.e., Section 806) applies to overseas employees of publicly traded companies. By this decision, the Supreme Court declined to challenge a ruling by the U.S. Court of Appeals for the First Circuit in January 2006. The First Circuit held that Section 806 does not apply outside the United States. The First Circuit stated that ‘[w]here, as here, a statute is silent as to its territorial reach, and no contrary congressional intent clearly appears, there is generally a presumption against its extraterritorial application.’ The First Circuit then concluded that there was no congressional intent to apply Section 806 outside the United States based on, among other things, the fact that Congress expressly provided for the extraterritorial application of Section 1107 of SOX, a criminal whistleblower statute.⁴ Similarly, several earlier decisions by administrative law judges in the U.S. Department of Labor limited the extraterritorial application of Section 806. However, in March 2005, in <i>Penesso v. Lee International, Inc.</i>, the administrative law judge held that an employee may bring a case under Section 806 if the case has a substantial nexus to the United States even though the employee was employed outside the United States. In <i>Penesso</i>, a substantial nexus to the United States was found to exist even though the employee was employed in Italy as the employee was a U.S. citizen and some of the protected activity and retaliation occurred in the United States.</p>

³ Section 806 of SOX added Section 1514A to Chapter 73 of Title 18 of the United States Code, to protect employees of publicly traded companies who provide evidence of fraud. Section 806 created an administrative complaint procedure and, ultimately, a federal civil cause of action intended to protect whistleblowing employees from retaliation or other discrimination by a publicly traded company. Section 806 provides that no company with a class of securities registered under Section 12 of the Exchange Act, or that is required to file reports under Section 15(d) of the Exchange Act, or any officer, employee, contractor, subcontractor or agent of such company, may discriminate against an employee in the terms and conditions of employment because of any lawful act done by the employee: (a) to assist in an investigation regarding any conduct that the employee reasonably believes constitutes a violation of 18 U.S.C. Section 1341, 1343, 1344 or 1348 (which concern, respectively, mail fraud, fraud by wire, radio or television, bank fraud and securities and commodities fraud), any SEC rule or regulation, or any provision of federal law relating to fraud against shareholders, when the assistance is provided to or the investigation is conducted by (i) a federal regulatory or law enforcement agency, (ii) any member of Congress or any committee of Congress, or (iii) a person with supervisory authority over the employee (or other person working for the employer who has the authority to investigate, discover or terminate misconduct); or (b) to assist in a proceeding filed or about to be filed (with any knowledge of the employer) relating to an alleged violation of 18 U.S.C. Section 1341, 1343, 1344 or 1348, any SEC rule or regulation, or any provision of federal law relating to fraud against shareholders. To

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
8. Audit Committee Financial Expert. Disclose in annual reports whether or not the audit committee includes at least one member who is a financial expert and if not, why not.	Yes. Disclose in Forms 20-F and 40-F.
9. Code of Ethics for CEO and Senior Financial Officers. Disclose in annual reports whether the company has adopted a code of ethics for the CEO, CFO, principal accounting officer or controller, or persons performing similar functions and if not, why not.	Yes. Include disclosure in Forms 20-F and 40-F.
Additionally, the company must promptly disclose any change in, or waiver of, the code of ethics.	<p><u>U.S. issuers:</u> Disclose changes to, and waivers of, the code of ethics on Form 8-K or on the company's web site within 4 business days after the change or waiver. For a company to use its web site for this disclosure, it must have disclosed in its most recently filed annual report: (a) that it intends to disclose changes and waivers on its Internet web site, and (b) its web site address.</p> <p><u>Non-U.S. issuers:</u> Disclose changes to, and waivers of, the code of ethics during the past year on Forms 20-F and 40-F. Disclosure in a Form 6-K or on the company's web site is encouraged, but not required. If disclosure is made by Form 6-K or web site posting within 4 business days after the change or waiver and otherwise meets the requirements for web site posting by U.S. issuers, no additional disclosure need be included in the annual report.</p>

obtain relief under Section 806, an aggrieved employee must file a complaint with the U.S. Secretary of Labor within 90 days of the date on which the alleged retaliation occurred. If the Secretary of Labor has not issued a final decision within 180 days of the filing of the complaint, and the delay is not due to the bad faith of the aggrieved employee, an action may be brought by the employee in the appropriate federal district court. Under Section 806, if a whistleblower prevails under the administrative process or in court, he is entitled to all relief necessary to make him whole, including: (a) reinstatement with the same seniority; (b) payment of back pay with interest; and (c) compensation for any special damages, including litigation costs, expert witness fees and reasonable attorney fees.

In 2002, President Bush stated that Section 806 protects employees who speak to a congressional committee during an investigation, but not when evidence is given to individual lawmakers or aides. Two senators criticized this statement as suggesting too narrow an application of Section 806.

⁴ Oxford Journals, Law, Capital Markets Law Journal, Volume 1, Issue 2, Pp. 245-250, available at <http://cmlj.oxfordjournals.org/content/1/2/245.full>.

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
10. Non-GAAP Financial Measures. Enhanced disclosure for press releases (Regulation G) and SEC filings.	Yes – but this additional disclosure does <i>not</i> apply to Canadian issuers using Form 40-F. Regulation G does not apply to a foreign private issuer if: (1) its shares are listed outside the United States, (2) the non-GAAP measure is not based on a measure calculated under U.S. GAAP, and (3) the non-GAAP measure is disclosed outside the United States (even if a contemporaneous or later public or web site disclosure is made in, but not targeted to investors in, the United States or the information is later included in a Form 6-K).
11. Earnings Releases to be Furnished on Form 8-K within 4 business days. Under Item 2.02 of Form 8-K, U.S. issuers must furnish to the SEC within 4 business days earnings releases or other announcements disclosing material non-public financial information about completed annual or quarterly fiscal periods. ⁵	No.
12. MD&A Disclosure of Off-Balance Sheet Arrangements and Aggregate Debt Obligations.	Yes. Disclose in Forms 20-F and 40-F.
13. Ban on Trading by Directors and Officers during Pension Fund Blackout Periods. ⁶	Yes. Blackout notices are filed on Form 8-K for U.S. issuers and as exhibits to Forms 20-F and 40-F for foreign private and Canadian issuers.

⁵ There is an exception from this requirement for Regulation FD-compliant follow-up announcements made within 48 hours after the initial public earnings announcement if: (1) the initial announcement was furnished on Form 8-K, (2) the follow-up announcement is made publicly available by webcast or similar technology, and (3) the relevant information is posted on the issuer's web site.

⁶ Section 306(a) of SOX was intended to prevent directors and executive officers from engaging in transactions involving issuer equity securities when other employees cannot. Generally, it prohibits any director or executive officer of a reporting issuer from acquiring or transferring any equity security of the issuer (other than an exempted security) during any pension plan blackout period for that equity security if the director or executive officer acquired the equity security in connection with his service or employment as a director or executive officer. Section 306(a) also requires an issuer to timely notify its directors and executive officers and the SEC of a blackout period.

Under Section 306(a) of SOX, the SEC adopted rules regulating securities trades by insiders during pension fund blackout periods (i.e., Regulation Blackout Trading Restriction (Regulation BTR)). Regulation BTR consists of five rules. These rules: (a) define terms used in SOX Section 306(a) and Regulation BTR; (b) clarify the operation of the Section 306(a) trading prohibition and provide several exemptions from the prohibition; (c) describe the exceptions to the definition of "blackout period" set forth in Section 306(a)(4)(A) of SOX; (d) clarify the operation of the private remedy for a violation of the Section 306(a) trading prohibition, including how to calculate recoverable profits; and (e) set forth the content and delivery requirements for notice of a blackout period.

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
<p>14. Strengthened Auditor Independence Requirements and Record Retention. Additional circumstances where auditors lose independence, auditors are prohibited from providing some non-audit services, audit committee pre-approval required for some services, rotation periods for audit partners, auditor report to audit committee of critical accounting policies and alternative GAAP treatment and retention of audit workpapers.</p>	<p>Yes. Generally applies to foreign private issuers and foreign accounting firms that conduct audits of: (1) foreign private issuers, and (2) foreign subsidiaries or affiliates of U.S. issuers.</p>
<p>15. Attorney Conduct Rules. Attorneys appearing and practicing before the SEC must report material violations of federal or state securities laws or fiduciary duties by a client issuer “up the ladder.”</p>	<p>A “non-appearing foreign attorney” does not appear and practice before the SEC. A “non-appearing foreign attorney” is: (1) admitted to practice law outside the United States, (2) does not hold himself out as practicing U.S. federal or state securities or other laws, and (3) conducts activities that would otherwise constitute appearing and practicing before the SEC only incidentally to, and in the ordinary course of, the foreign law practice or only in consultation with a U.S. attorney. The scope of the work typically performed by most foreign attorneys should enable them to qualify for this exemption. Additionally, attorneys practicing outside the United States are not required to comply with the requirements of the attorney conduct rules “to the extent that such compliance is prohibited by applicable foreign law.”</p>

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
<p>16. Accelerated Filing Deadlines for accelerated filers filing Forms 10-K and 10-Q to 60 (from 90) and 35 (from 45) days after period end.</p> <p>Currently, an annual report on Form 10-K must be filed: (1) within 60 days after the end of the fiscal year if the issuer is a large accelerated filer, (2) within 75 days after the end of the fiscal year if the issuer is an accelerated filer, and (3) within 90 days after the end of the fiscal year for all other registrants.</p> <p>Currently, a quarterly report on Form 10-Q must be filed by the issuer after the end of each of the first three fiscal quarters of each fiscal year as follows: (1) within 40 days after the end of the fiscal quarter if the issuer is a large accelerated filer or an accelerated filer, and (2) within 45 days after the end of the fiscal quarter for all other registrants.</p>	<p>No, but the SEC has accelerated the Form 20-F filing deadline to within 4 months after the end of the fiscal year covered by the report, for fiscal years ending on or after December 15, 2011 (from within 6 months after the end of the fiscal year covered by the report, for fiscal years ending before December 15, 2011).</p>
<p>17. Web Site Posting of Exchange Act Reports. Disclose whether posting and if not, why not.⁷</p>	<p>No.</p>

⁷ Specifically, accelerated filers and, currently, large accelerated filers, must disclose in their annual reports on Form 10-K the following: (1) the issuer's web site address (URL), if it has one; (2) whether the issuer makes available free of charge through its web site, if it has one, its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports filed or furnished under Section 13(a) or 15(d) of the Exchange Act, as soon as reasonably practicable after electronic filing or furnishing to the SEC; and (3) if the issuer does not make its filings available through the Internet: (a) the reasons why it does not do so (including, where applicable, that it does not have an Internet web site), and (b) whether it voluntarily will provide electronic or paper copies of its filings free of charge upon request.

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
<p>18. Management Assessment of Internal Controls. Extends disclosure to management evaluation of internal controls. Requires annual evaluation and attestation by auditors of internal controls. Specifically, if the issuer is an accelerated filer or a large accelerated filer, its annual report must include an independent auditor's attestation report on management's assessment of the issuer's internal control over financial reporting. (Under former SEC rules, a non-accelerated filer would have been required to include an attestation report of its independent auditor on internal control over financial reporting in the filer's annual report filed with the SEC for fiscal years ending on or after June 15, 2010. However, in September 2010, the SEC removed the requirement for a non-accelerated filer to include in its annual report an attestation report of the filer's independent auditor.)</p>	<p>Yes. Disclosure is required annually on Forms 20-F and 40-F.</p>
<p>19. Audit Committee Independence, Responsibilities and Authority, and Procedures for Handling Complaints. Implemented by Rule 10A-3 under the Exchange Act and exchange corporate governance standards.</p>	<p>Yes. Applies to foreign private issuers, subject to exemptions from certain provisions to address special home country requirements.</p>
<p>20. Improper Influence of Auditors. Prohibits any officer or director, or anyone acting under their direction, from improperly influencing auditors if such person knows or should know that his action could render the issuer's financial statements materially misleading.</p>	<p>Yes.</p>
<p>21. Disclosure of Audit Fees.</p>	<p>Yes. Disclosure in Forms 20-F and 40-F.</p>

RULES	APPLICABILITY TO FOREIGN PRIVATE AND CANADIAN ISSUERS
<p>22. Shareholder Approval of Equity Compensation Plans. Generally, the NYSE rule requires shareholder approval of all equity compensation plans and all material plan revisions. Plans adopted before June 30, 2003 do not require shareholder approval unless they are materially revised. Additionally, brokers may not give a proxy to vote on equity compensation plans unless the beneficial owners have given voting instructions.</p> <p>Under the NASDAQ rule, shareholder approval is required before issuing securities when a stock option or purchase plan is to be established or materially amended or other equity compensation arrangement made or materially amended, under which stock may be acquired by officers, directors, employees or consultants, subject to certain exceptions.</p>	<p>No.</p> <p>NYSE listed companies that are foreign private issuers are permitted to follow home country practice in lieu of this provision of the NYSE corporate governance standards.</p> <p>A foreign private issuer listed on NASDAQ may follow the practice in that company's home country in lieu of NASDAQ's corporate governance requirements, subject to several important exceptions which do <i>not</i> include the requirement concerning shareholder approval of equity compensation plans. A foreign private issuer that elects to follow home country practice in lieu of a NASDAQ corporate governance requirement must submit to NASDAQ a written statement from an independent counsel in that company's home country certifying that the company's practices are not prohibited by the home country's laws. For new listings, this certification is required at the time of listing. For listed companies, the certification is required at the time the company seeks to adopt its first non-compliant practice.</p>