Client Advisory

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SEC Updates Guidance to Determine "Foreign Private Issuer" Status

The integrated disclosure system of the U.S. Securities and Exchange Commission (the "SEC") makes important accommodations for foreign private issuers ("FPIs"). The SEC recently released a number of Compliance and Disclosure Interpretations ("C&DIs") that clarify and facilitate the determination of FPI status[1] under both the Securities Act of 1933, as amended (the "Securities Act"), and the Securities Exchange Act of 1934, as amended (the "Exchange Act"). This Advisory describes the application of the FPI status tests as expanded under the recent C&DIs.

The regulatory accommodations to FPIs include:

- Ability to choose for its financial reporting among U.S. generally accepted accounting principles ("U.S. GAAP"), International Financial Reporting Standards ("IFRS") or local GAAP (reconciled to U.S. GAAP).
- Filing of annual reports on Form 20-F (or 40-F for certain Canadian filers) rather than on Form 10-K. Such reports are due 120 days after the end of the fiscal year.
- No Form 10-Q quarterly reporting or Form 8-K current reporting obligations; instead Form 6-K is used.
- No insider reporting and disgorgement rules.
- No requirement to file U.S. proxy statements.

An FPI is defined under the Securities Act and the Exchange Act as an issuer incorporated in a non U.S. jurisdiction (other than a foreign government and its political subdivisions) that meets either of the following tests :

1. 50% or less of its outstanding voting securities are held of record by U.S. residents, or
2. more than 50% of its outstanding voting securities are held of record by U.S. residents but does not have any one of the following:

   (i) a majority of its executive officers or directors are U.S. citizens or residents, or
   (ii) more than 50% of its assets are located in the U.S. or
   (iii) its business is principally administered in the U.S.

[1] See C&DI Questions 203.17 to 203.23 to the SEC's Securities Act Rules and Questions 110.02 to 110.08 to Exchange Act Rules.

The first FPI test relates to the extent of a registrant's U.S. share ownership, and the second test relates to the level of a registrant's U.S. business contacts.

Timing of Determination. A company must determine its status as an FPI annually, as of the end of its second fiscal quarter (i.e., typically June 30th). In the case of a new registrant with the SEC, the determination of whether a company is an FPI will be made as of a date within 30 days prior to the company's filing of an initial registration statement.

Ramifications of Loss of FPI Status. If a company determines that it no longer qualifies as a FPI as of the end of its second fiscal quarter, it must transition to U.S. issuer reporting status and become subject to the reporting requirements, rules and forms for a U.S. company beginning on the first day of the next fiscal year, i.e., typically January 1st. A company may re-qualify as an FPI as of the end of its second fiscal quarter in the next fiscal year, provided it then meets one of the FPI tests.

Process for determining U.S. share ownership (1st test). The company must review the addresses of its registered shareholders and also look beyond "street name" accounts held of record by a broker-dealer, bank or nominee, and determine the number of accounts located in the U.S., the number of accounts in other countries and the outstanding voting securities for each account. In the recent CD&Is, the SEC clarified that a person with a permanent resident status (i.e., Green Card holder) is assumed to be a U.S. resident. Importantly, even other persons without such permanent residency may be deemed U.S. residents for this test based upon factors such as tax residency, nationality, mailing address, physical presence, location of a significant portion of their financial and legal relationships or immigration status. [2]

When conducting shareholder counts, FPIs must ensure they apply a consistent set of criteria (not changing them to achieve a desired result), which may include the previously mentioned factors. Companies may rely in good faith on information supplied by a broker, bank or nominee. If, after reasonable inquiry, the company is unable to obtain information about the amount of securities represented by accounts of customers resident in the United States, it may assume that these customers are residents of the jurisdiction in which the nominee has its principal place of business.

Process for determining levels of business contacts under each prong (2nd test).

i. Whether a Majority of Executive Officers or Directors Are U.S. Citizens or Residents. The recent CD&Is clarified that this process involves four separate determinations: the citizenship of executive officers, the residency of executive officers, the citizenship of directors and the residency of directors.

ii. Whether the Majority of an Issuer's Assets Are Located in the United States. The SEC explained in the recent CD&Is that the registrant may rely on the geographic segment information as reported in its

[2] These factors are also used to determine whether a natural person is a resident of the U.S. for purposes of the definition of "US person" under Regulation S, which provides a safe harbor exemption from registration under the Securities Act for certain offshore offerings and sales of securities.

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financial statements or on another reasonable methodology, as long as the methodology used is consistently applied.

iii. Whether a Company's Business Is Administered Principally in the United States. The determination of the geographic administration of the business (inside or outside the U.S.), according to the CD&Is, is an exercise of judgment by the issuer. No single factor or group of factors are conclusive. For example, holding shareholder or board meetings in the U.S. is not by itself the determination. The company must assess on a consolidated basis the location from which its officers primarily direct, control and coordinate the company's activities.

The process of determining the level of business contacts is based on judgment calls that must be consistently applied. In conducting its annual FPI status examination, unless the company meets the first test by a convenient safe margin, it should also monitor the second test's levels of business contacts closely for comfort that it will maintain its FPI status. We suggest that you consult with U.S. counsel throughout the process, especially before the critical date of determination (the end of the company's second fiscal quarter) after which the determination cannot be reversed until the end of the second fiscal quarter in the next fiscal year as there is no grace period once the determination is made.

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