

Securities and Exchange Commission Proposes Revisions to the Cross-Border Tender Offer, Exchange Offer, and Business Combination Rules

by William L. Tolbert, Jr. and Elaine Wolff

Executive Summary

Offerors in cross-border transactions who wish to avoid being subject to U.S. regulations, including having to prepare and file a registration statement, or who face conflicts between U.S. and foreign laws have frequently excluded U.S. investors from participating in these transactions. On May 6, 2008, the SEC sought to encourage offerors to include U.S. holders by proposing rule changes to expand the current cross-border exemptions from U.S. tender offer rules and from the registration requirements of Section 5 of the Securities Act of 1933 ("Securities Act"). The proposed revisions do not address the fact that existing regulations subject foreign issuers to potential exposure under the anti-fraud and civil liability provisions of U.S. federal securities laws, even where transactions involve relatively modest U.S. holdings.

An offeror's eligibility to rely on the cross-border exemptions depends in part on the type of transaction, whether the target is a foreign private issuer and the amount of U.S. holdings in the target's securities. Most significantly, the proposed changes would make it easier for offerors to rely on the cross-border exemptions by clarifying and adding some flexibility to the tests for calculating U.S. ownership of the target. The rules would also encourage offerors to include U.S. holders by

- (i) expanding relief from the heightened disclosure requirements applicable to going private transactions by affiliates,
- (ii) extending relief where target securities are not subject to Rule 13e-4 or Regulation 14D of the Securities Exchange Act of 1934 ("Exchange Act"),
- (iii) eliminating certain conflicts between U.S. and foreign law, and
- (iv) allowing certain purchases of target securities outside of a tender offer.

Procedurally, the rules would require all Forms CB (English translation of the offer materials) and the accompanying Forms F-X (for appointing an agent in the U.S. for service of process) to be filed electronically, modify the cover pages of certain tender offer schedules and registration statements to list any cross border exemptions relied upon, and permit foreign institutions to report on Schedule 13G to the same extent as their U.S. counterparts.

In its lengthy release, the SEC has solicited comments on a number of questions. The 45 day comment period ends on June 23, 2008.

What is the purpose of the rule?

The proposed rule is intended to encourage offerors and issuers in cross-border business combinations to allow U.S. investors to participate in these transactions as well as in rights offerings by foreign private issuers. To encourage offerors to include U.S. holders, the proposed rules attempt to address conflicts with foreign regulations and practice and codify existing interpretive positions in the cross-border area.

When is a cross-border business combination exempt from U.S. regulation?

The cross-border exemptions are available in connection with qualifying transactions in which the target company is a “foreign private issuer” (as defined in Exchange Act Rule 3b-4(c)) and in rights offerings where the issuer is a foreign private issuer. The offeror need not be a foreign private issuer and may, in fact, be a U.S. company. Whether a “business combination” qualifies as a transaction that would not be subject to U.S. regulation depends in part on whether the transaction is one of the following: (i) a tender or exchange offer, (ii) merger, statutory amalgamation, arrangement or reorganization requiring the vote of security holders of one or more participating companies, or (iii) a statutory short form merger that does not require a vote of security holders.

In general under current rules, a cross-border transaction is exempt from most U.S. tender offer rules and from the registration requirements of Section 5 of the Securities Act where U.S. holders own no more than ten percent of the target company’s non-affiliated float (“Tier I”). Where U.S. holders own more than ten percent but no more than 40 percent of the target’s non-affiliated float (“Tier II”), the cross-border exemptions provide relief from some tender offer rules, such as prompt payment and extension and notice of extension requirements, but do not provide relief from the registration requirements of Section 5. Transactions in which U.S. holders own more than 40% of the target’s non-affiliated float are subject to the same rules that apply to domestic offers. Significantly, in this proposing release the SEC has requested comment on whether the Tier I threshold should be increased from 10% to 15%.

How do the proposed rules change the test for calculating U.S. ownership?

The proposed rules would change the test for calculating U.S. ownership of the target company in three ways.

1. Permit offerors to calculate U.S. ownership within a specified 60-day range.

In order to determine whether target securities are held by persons resident in the U.S., offerors in negotiated transactions are required to “look through” securities held of record by nominees to identify those held for accounts of persons located in the U.S. Currently the rules require that the calculation be made as of a single date which is the 30th day before the commencement for a tender or exchange offer, or before the solicitation for other kinds of business transactions. It can be difficult in some countries to complete the look-through analysis in 30 days and as of a specific date. The proposed rules expand the time period to allow calculation on any day within a 60-day period before public announcement of the business combination. The expanded time period and allowance to permit the offeror to select the most advantageous date within the 60 day window is intended to provide greater flexibility to offerors who may encounter problems in the time needed to determine whether target securities are held by persons resident in the U.S. or who need more time to prepare offering materials or complete the regulatory review process. Nevertheless, the continued use of the “look through” test means that as companies contact nominees and other holders of record to conduct the “look through” test, they must manage the risk that the transaction will be prematurely disclosed.

2. Use the date of public announcement of the business combination as the reference point for calculating U.S. ownership.

Currently, the triggering event for calculating U.S. holders is the date of commencement. The proposal to use the date of announcement as the triggering event is intended to enable offerors to determine at an earlier point how they will treat U.S. holders and to provide this information to investors at an earlier stage. Investors who acquire target shares after announcement would be able to determine whether

they will have the full protections of the tender offer rules. Further, offerors would be able to meet home country requirements which often mandate that they include information about the treatment of U.S. holders in the announcement of the transaction. This change also helps to alleviate the problem created by keying the “look through” analysis to commencement for purposes of the exemption from Rule 14e-5. Rule 14e-5 prohibits purchases of target securities outside of the tender offer from the date of announcement through its expiration. The problem is that an offeror will not necessarily know at the time of announcement whether it will qualify for the cross border exemptions as of the 30th date before commencement.

3. Specify when the offeror has “reason to know” information about U.S. ownership that may affect its ability to rely on the presumption of eligibility in hostile tender offers.

Because third parties face difficulties in obtaining information about U.S. ownership without the cooperation of the target, the current cross-border exemptions allow an offeror in hostile tender offers to presume eligibility to rely on the exemptions. The hostile presumption is based in part on a comparison of trading volume of the target’s securities in the U.S. to worldwide trading volume rather than nationality of beneficial owners. Currently, the presumption of U.S. ownership is qualified if the offeror knows or “has reason to know” that the actual level of U.S. ownership of the target securities exceeds the relevant thresholds for Tier I and Tier II. To help alleviate uncertainty about whether unsolicited offerors must seek out information about U.S. ownership levels and what constitutes “reason to know,” the proposed rules would specify that an offeror has “reason to know” information that is publicly available, including information about beneficial ownership reports filed by third parties. Further, as proposed, offerors may not ignore credible information received *before* announcement about target securities held by U.S. persons from non-public sources, such as investment bankers or other market participants from whom they receive information. Post-announcement developments need not be taken into account.

How do the proposed rules expand relief under Tier I for certain affiliated going private transactions?

The proposed rules expand the kinds of cross-border transactions that qualify for the Tier I exemption in connection with going private transactions subject to Rule 13e-3 of the Exchange Act. Rule 13e-3 establishes heightened filing and disclosure requirements for affiliated transactions that have the effect of causing the target to become a private company because of conflicts of interest inherent in these situations. Currently, the scope of the Tier I exemption from Rule 13e-3 does not apply to cash mergers, compulsory acquisitions for cash, court-approved business combination transactions and other types of transactions. The proposed rules remove all restrictions on the category of transaction covered.

How do the proposed rules expand relief for Tier II transactions?

The proposed rules clarify that the Tier II exemptions are available regardless of whether the target securities are subject to Rule 13e-4 or Regulation 14D. Regulation 14D applies to offers where the subject security is registered under Section 12 of the Exchange Act and Rule 13e-4 applies to issuer tender offers where the subject securities are not registered under section 12 but where the issuer has another class of securities that are so registered.

How do the proposed rules eliminate certain conflicts between U.S. and foreign law and practice?

1. Expand Tier II cross-border exemptions to multiple non- U.S. offers.

Currently, the Tier II exemptions allow an offeror to separate the offer for the same securities into two offers – one in the U.S. and one foreign. The exemption for dual offers is intended to provide offerors with flexibility to comply with two sets of regulatory regimes and to deal with conflicts in tender offer practice between the U.S. and foreign jurisdictions. The change is intended accommodate situations in which more than two offers may be needed such as where the primary trading market for the target’s securities differs from the target’s country of incorporation.

The proposed rules clarify that offerors who conduct separate U.S. and non-U.S. offers for less than all of a class of target securities must use a single proration “pool.” Currently, to assure equal treatment of security holders who have tendered their securities, the rules require tendered securities to be purchased on a pro rata basis if a partial tender offer is oversubscribed. In the context of U.S. and non-U.S. offers, this clarification regarding a single “pool” is intended to assure that offerors do not use different proration factors which could disadvantage U.S. holders as compared to holders tendering into foreign offers.

2. Allow offerors to include foreign holders in U.S. offers and U.S. holders in foreign offers.

Currently, the Tier II dual offer exemption provides that the U.S. offer can be open only to security holders resident in the U.S. This limitation creates a problem for offerors who want to include all holders of American Depositary Receipts (ADRs), not only U.S. holders, in the U.S. offer. Similarly, the existing Tier II dual offer provision requires that the foreign offer be available only to non-U.S. holders. The prohibition against permitting U.S. holders from participating in the foreign offer may conflict with the law of the target’s home country if those rules do not permit the exclusion of any security holders, including U.S. holders. The rules would provide that one or more foreign offers could be conducted in conjunction with a U.S. offer for the same securities. U.S. persons could be included in foreign offers only where the law of the jurisdiction governing such foreign offer expressly precludes the exclusion of U.S. persons from the foreign offer and where U.S. holders are provided with disclosure about the risks of participating in the foreign offer.

3. Permit the suspension of “back-end” withdrawal rights while tendered securities are counted but before they are accepted for payment.

Currently, offerors are required to provide withdrawal rights after a set date, measured from the commencement of the tender offer until shares have been accepted for payment. Offerors may not accept tendered securities until all offer conditions have been satisfied or waived and the counting process is complete. However, in other countries offerors may not know whether the minimum tender condition has

been satisfied immediately after the end of the initial offering period. In recognition of this fact, the new rules would allow, under certain conditions, withdrawal rights to be terminated at the end of an offer and during the counting process for offerors that do not provide a subsequent offering period.

4. Eliminate the time limit for subsequent offerings.

This is intended to alleviate conflicts where foreign law or practice requires a longer period than our current 20 day maximum limit on the length of a subsequent offering. The rules would provide an opportunity for remaining holders to tender into a successfully-consummated offer, after which the market for target securities may be very limited.

5. Expand relief for subsequent offering periods.

The new rules would allow securities tendered during a subsequent offering period to be purchased up to 14 days after the date of the tender, allow separate offset and proration pools for securities tendered during initial and subsequent offering periods, and allow the payment of interest on securities tendered during a subsequent offering period if required under foreign law. The proposed changes are needed because of conflicts with the tender offer rules requiring prompt payment and equal treatment. The proposal recognizes that in many foreign jurisdictions prompt payment is practically unworkable and payment of interest on securities is required during the subsequent offering period. The proposed rules would permit offer structures consisting of mixed offers of cash and securities with the option to elect a different proportion of cash and securities to the extent that other holders make opposite elections.

6. Allow offerors to early commence.

The proposed rules allow offerors for foreign securities that are not registered under the Exchange Act to take advantage of early commencement by commencing their exchange offer upon the filing date of the registration statement. Early commencement is available only to exchange offers for target securities that are registered under Section 12 of the Exchange Act. The proposed rule is intended to address situations where offerors are unable to early commence because of foreign jurisdiction

requirements that offers must include all classes of securities that are convertible into the subject securities even if such class is not registered under Section 12 of the Exchange Act.

How do the proposed rules expand the ability to make purchases outside the tender offer?

Currently, Tier I tender offers for securities of foreign private issuers are exempted from Exchange Act Rule 14e-5. Rule 14e-5 prohibits offerors from making purchases outside of the offering from the time of announcement until the offer expires, which is a common event outside the U.S. The rule protects investors by preventing an offeror from extending greater or different consideration to some holders by offering to purchase their shares outside the offer, while other holders are limited to the offer's terms. The proposed rules would codify commonly provided exemptive relief for Tier II tender offers that permits purchases in a foreign tender offer made concurrently with a U.S. offer. This relief would be conditioned upon (i) treatment of U.S. holders at least as favorably as non-U.S. holders, (ii) disclosure in U.S. offering documents of the offeror's intent to make purchases, and (iii) purchases in foreign tender offers only. To

address situations where the target is a non-U.S. company, the majority of whose shareholders reside outside the U.S., the rules also would permit purchases in the open market or privately negotiated purchases outside the U.S. by (i) an offeror and its affiliates; and (ii) an affiliate of a financial advisor under certain conditions. The conditions would require disclosure in U.S. offering documents of the offeror's intent to make purchases in a foreign offer and would require that the tender offer price be raised to equal any higher price paid outside of the tender offer. There are additional conditions where an affiliate of a financial advisor purchases or arranges to purchase outside of a tender offer.

What filing changes are required by the proposed rules?

The proposed rules would require all Forms CB and the accompanying Forms F-X to be filed electronically. The rules would also modify the cover pages of certain tender offer schedules and registration statements to list any cross border exemptions relied upon, and permit foreign institutions to report on Schedule 13G to the same extent as their U.S. counterparts.

For more information, please contact the following Jenner & Block attorneys:

William L. Tolbert, Jr.

Partner

Tel: 202 639-6038

Email: wtolbert@jenner.com

Elaine Wolff

Partner

Tel: 202 637-6389

Email: ewolff@jenner.com