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FOREIGN PRIVATE ISSUERS

Foreign Companies May Receive, as "Foreign Private Issuers," Significant Accommodations Under U.S. Securities Laws, if They Can Pass Either a Shareholder or a Three-part Business Test. The Author Reviews the Tests, the Guidance Provided by the SEC Staff, and the Advance Planning Needed if Foreign Private Issuer Status Is Lost.

By Sandra Folsom Kinsey

The Securities and Exchange Commission (SEC) makes important regulatory accommodations for "foreign private issuers" but not every foreign company is covered by that term. Even companies that have satisfied the definition of "foreign private issuer" in the past may find that corporate developments have changed their answers to one or more of the definitional tests. In particular, the recent wave of cross-border M&A activity may have put some companies' foreign private issuer status in jeopardy. Losing foreign private issuer status can have serious consequences for a non-U.S. company. This article explains the SEC's special definition of the term "foreign private issuer" and provides guidance for evaluating a non-U.S. company's status under that definition.

The SEC historically has used the term "foreign private issuer" to determine which companies are eligible for certain accommodations under the U.S. federal securities laws. Not every foreign company is a "foreign private issuer."[1] A company may be incorporated outside the United States, but have enough U.S. business contacts and shares held by U.S. residents that the SEC considers it to be an "essentially U.S. issuer."[2] These "essentially U.S." foreign companies are subject to the same regulations as a company incorporated in the United States. Foreign companies may not be aware of the importance of this distinction, but significant consequences flow from whether or not a company satisfies the SEC's definition of a "foreign private issuer." Recent changes to part of the foreign private issuer definition also mean that non-U.S. companies now must take additional steps to determine whether they fall within the definition.

Why does it matter whether a company is a "foreign private issuer"?

The SEC has made significant formal and informal accommodations for foreign private issuers. The following are some of the more important accommodations.

- No SEC requirement for quarterly or other interim reporting.[3]
- No requirement to comply with the SEC's rules for proxy solicitations in connection with shareholder meetings or follow the SEC rules for presenting shareholder proposals.[4]

1. The definition of "foreign private issuer" is found in Rule 405 under the Securities Act of 1933, as amended (Securities Act), and in Rule 3b-4 under the Securities Exchange Act of 1934, as amended (Exchange Act). The use of the word "private" sometimes causes confusion. It is intended to make a distinction between private-sector, commercial entities and public-sector, governmental entities, and does not refer to whether the company is publicly traded or not.

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2. See Release No. 33-6493 (Oct. 6, 1983) [48 FR 46736]. The SEC considers that if a foreign company has sufficient contacts with the United States, there is an important U.S. public interest in the company that justifies treating it the same as a U.S. company for regulatory purposes. See Release No. 33-6433 (Oct. 28, 1982) [47 FR 50292].

3. Although the SEC does not require quarterly reporting by foreign private issuers, U.S. stock exchanges or the Nasdaq Stock Market may require a half-yearly report. In addition to annual reports, the SEC requires foreign private issuers to submit a copy of any material information they file, make public or disclose to shareholders outside the United States, under cover of Form 6-K.

- Annual reports are due within six months after fiscal year end, instead of the 90-day deadline for U.S. domestic companies.

- Officers, directors and ten percent shareholders are not required to file reports of beneficial ownership under Section 16 of the Exchange Act,[5] although beneficial ownership reports may be required under Section 13 of the Exchange Act.[6]

- No "short-swing" trading liability is imposed on insiders who purchase and sell securities within a six-month period.[7]

- More limited compensation disclosure is required, and there is no requirement to disclose individual compensation unless it is disclosed publicly elsewhere.

- No requirement to apply U.S. generally accepted accounting principles (GAAP) to the company's primary financial statements, although reconciliation to U.S. GAAP will be required.

- Free choice of which reporting currency to use in presenting the company's financial statements.[8]

- No requirement to comply with Regulation FD, the SEC's new prohibition on selective disclosure of material information.[9]

- No requirement to establish a formal audit committee with the duties specified in SEC rules.[10]

- On an informal basis, the SEC permits submission of "draft" offering documents for confidential review before a public filing is made.[11]

- Companies are eligible for a special exemption from Exchange Act registration and reporting if they have made no affirmative efforts to enter the U.S. capital markets. Claiming this exemption permits foreign private issuers to establish "Level 1" American Depositary Receipt (ADR) programs.[12]

- Fewer restrictions on offers and sales of securities outside the United States for companies relying on the SEC's Regulation S "safe harbor" from the U.S. registration requirements.

When a company loses its foreign private issuer status, the consequences are immediate. Among other things, the company's corporate communications are subject immediately to the selective disclosure prohibitions of Regulation FD. Officers, directors and major shareholders must file initial reports of beneficial ownership within ten days after the event that causes these insiders to be subject to Section 16. The "event" in this case would be the company's determination that it no longer is a foreign private issuer.[13] The company's first quarterly report on Form 10-Q will be due 45 days after the

4. In fact, the SEC staff has taken the position in its no-action letter "Proxy Materials of Foreign Private Issuers" (avail. March 10, 1992) that foreign private issuers may not file proxy or information statements under Section 14, even if they voluntarily choose to file periodic reports on the forms designated for U.S. domestic issuers. As a result, a foreign private issuer that voluntarily files annual reports on Form 10-K may not incorporate the information required by Part III of Form 10-K by reference to a subsequently filed proxy statement.

5. Under Section 16 of the Exchange Act, a company's officers and directors and the beneficial owners of more than ten percent of its equity securities must file individual reports of their transactions and holdings involving the company's equity securities. The reporting obligation is imposed directly on the individual members of management and shareholders rather than on the company, but in practice many companies assist officers and directors with the reporting requirements.

6. Under Section 13 of the Exchange Act, the beneficial owner of more than five percent of any class of equity securities registered under Section 12g of the Exchange Act must file a report of beneficial ownership. Unlike Section 16, there is no exemption from this reporting requirement if the issuer of the securities is a foreign private issuer.

7. See Exchange Act Rule 3a12-3(b). Section 16 imposes liability on officers, directors and ten percent owners for any profits realized by them on any purchase and sale, or sale and purchase, of the company's equity securities within a six-month period. The formula for matching purchases and sales is applied mechanically by most courts and does not depend on whether the reporting person actually realized a profit or acted on inside information.

8. See Item 3-20 of Regulation S-X.

9. Regulation FD ("fair disclosure"), which went into effect on October 23, 2000, attempts to "level the playing field" for investors by requiring that a company and persons acting on its behalf simultaneously disclose to the public any material nonpublic information that is made available to market professionals.

10. The SEC requires proxy statements to include a report from the audit committee regarding its discussions with the company's outside auditors, as well as information about the independence of the committee members. See Item 7 of Schedule 14A.

11. This staff practice, which is of great help in meeting offering timetables and ensuring uniform disclosure in all jurisdictions where the offer is made, is available only for foreign private issuers.

12. See Exchange Act Rule 12g3-2(b). A company with more than $10 million in assets and more than 500 holders of its equity securities worldwide (including, for foreign companies, more than 300 U.S. holders of its equity securities) is required to register under Section 12(g) of the Exchange Act and file periodic reports. Foreign private issuers who have not made an affirmative effort to enter the U.S. securities markets (i.e., have not listed shares on a U.S. stock market or filed a Securities Act registration statement) are eligible for the Rule 12g3-2(b) exemption from registration and reporting. The company must claim the exemption before it passes the 300 U.S. equity holders test. A company that claims this exemption and complies with its terms will be able to establish an ADR program for "over-the-counter" trading of its securities in ADR form (often referred to as a "Level 1" ADR program.) Claiming the exemption is not sufficient to permit the company's shares to trade on a national securities exchange, the Nasdaq Stock Market or the OTC Bulletin Board. While most of this article refers to the impact on reporting companies if they lose their foreign private issuer status, the consequences for a company relying on the Rule 12g3-2(b) exemption can be equally disruptive.

13. The SEC staff has taken the position that transactions by insiders prior to the company losing its foreign private issuer status generally will not be subject to the reporting or short-swing trading liability provisions of Section 16. The only exception is if the event that culminated in the company's loss of foreign private issuer status also involved an initial registration of equity securities under Section 12 of the Exchange Act. See no-action letter to Thelen, Marrin, Johnson & Bridges (avail. Dec. 23, 1994).

end of its current fiscal quarter. The company must report its financial statements in U.S. dollars and apply U.S. GAAP in preparing those statements. There is no "phase-in" period for the reporting currency and GAAP requirements, so they would apply to the company's first quarterly report. In addition, financial statements for prior periods must be restated on a U.S. GAAP basis.[14] Companies planning to offer securities in their home market, or anywhere else outside the United States, without U.S. registration will have to comply with the generally more restrictive Regulation S requirements that apply to U.S. companies.[15] While this article focuses primarily on companies registered with the SEC, ceasing to be a foreign private issuer may have a significant impact on unregistered foreign companies with securities trading in the U.S. "over-the counter" market. If those companies have relied on the special exemption from Exchange Act registration and reporting, they no longer will be eligible for that exemption and may find that they are required to register and begin reporting under the Exchange Act.[16]

These consequences are significant enough that advance planning is advisable to mitigate their effects, at least to the extent possible. If the change in status cannot be avoided, advance preparation will reduce the disruption that can result from discovering at an inopportune time that the company no longer may rely on the foreign private issuer accommodations. As a practical matter, a company may not decide to forego an otherwise attractive acquisition in the United States or relocate personnel or production facilities because of concern about the impact on the company's foreign private issuer status. The company can make more informed business decisions, however, and be better prepared for the consequences, if it understands the foreign private issuer definition and how it is applied.

14. See Remarks by Craig Olinger, Deputy Chief Accountant in the SEC's Division of Corporation Finance, at the 28th Annual National Conference on Current SEC Developments, December 6, 2000, available on the SEC website at www.sec.gov. Mr. Olinger also noted that in the company's first filing with U.S. GAAP financial statements, it should set out in full the accounting policies it has adopted under U.S. GAAP.

15. A company that ceases to be a foreign private issuer is treated like a U.S. company for purposes of Regulation S. Its offers and sales of securities outside the United States would be subject to one of the two more restrictive categories of the safe harbor. Under Rule 905 of Regulation S, any of its equity securities that are "restricted securities" in the United States would continue to be restricted when resold outside the United States.

16. Depending on when the company discovers that it is no longer eligible for the exemption, it may not be required to register immediately. The registration obligation is based on the company's assets and equity holders as of the end of its fiscal year, and the company has 120 days after fiscal year end to file its registration statement.

What is the SEC's definition of a "foreign private issuer"?

The definition of "foreign private issuer" has two parts, one based on the company's level of U.S. shareholdings and the other on its business contacts with the United States. A non-U.S. company may have to analyze both parts of the definition in order to determine whether it is a "foreign private issuer."

The shareholder test:

Are more than 50 percent of the company's outstanding voting securities held by U.S. residents?[17]

- If the answer is "no," the company qualifies as a foreign private issuer. It may end its analysis at this point, and does not have to apply the second test.
- If the answer is "yes," the company still may be a foreign private issuer, depending on its business contacts with the United States. It must apply the second definitional test.

The business contacts test:

Are a majority of the company's executive officers or directors U.S. citizens or residents?

or

Are more than 50 percent of the company's assets located in the United States?

or

Is the company's business administered principally in the United States?

- If the answer to all of these three questions is "no," the company is still a foreign private issuer, even if over 50 percent of its shares are held by U.S. residents.
- If the answer to any one of these three questions is "yes," these business contacts, together with the majority U.S. share ownership in the first test, will result in the company not being a foreign private issuer.

17. The SEC has never provided guidance on how to determine the "residency" of a company's shareholders. This issue usually does not present interpretive problems, but companies occasionally are faced with shareholders who, for example, reside half the year in the United States and half the year outside the United States. In this situation, the company should decide what criteria it will use in determining residency and then apply those criteria consistently. Whether the basis is tax residency, nationality, mailing address or some other test, the criteria should be applied consistently and not changed in order to achieve the desired result.

The SEC staff traditionally has not provided much guidance on how to apply these definitional tests, in part because any guidance the staff gives for one company might not apply to companies in a different industry. The burden is on the company itself to analyze whether or not it satisfies the "foreign private issuer" definition, although the SEC staff may challenge that analysis during the course of reviewing a filing. The best defense to a challenge of this sort may be to document how the definitional tests were applied at the time the analysis was made.

How must a company apply the shareholder test?

The SEC's recent changes to the "foreign private issuer" definition affect the test for whether more than 50 percent of a company's outstanding voting securities are held by U.S. residents.[18] Formerly, a company would look to the record owners of its securities to determine U.S. residency.[19] Effective September 30, 2000, however, a company must "look through" the record ownership of brokers, dealers, banks or other nominees that hold securities for the account of their customers, and determine the residency of those customers.[20] The change was based on the SEC's view that record ownership no longer gives a true picture of whether a non-U.S. company is entitled to the accommodations for foreign private issuers. The move beyond record ownership reflects changes in the way securities are held, including greater reliance on nominees and depositaries.

To apply this test, the company must "look through" record ownership in a maximum of three jurisdictions: the United States; the company's home country (i.e., the country in which it is incorporated or organized); and the jurisdiction where its primary trading market is located, if that is different than its home country.[21] The response to these inquiries may produce additional layers of nominees, and the inquiry should continue with those nominees. Some companies have asked how many layers of nominees they must look through to trace the residency of customer accounts. The SEC staff has declined to draw any precise lines, so companies are well-advised to keep making inquiries of successive layers of nominees until they reach a point where the information clearly is unavailable. The SEC has acknowledged that the information may not be available if, for example, the nominee is not able to provide the information, refuses to do so, or imposes an unreasonable charge for providing the information. In that case, the company may rely on a presumption that the residency of the nominee's customers is the same as the nominee's principal place of business.[22]

In all instances, the company is expected to make a good faith effort to obtain the information. Even if a nominee refuses to provide detailed information such as the identity and residency of individual customers, it still may be willing to provide general information such as the total number of shares it holds as nominee and the percentage of those shares held by customers with U.S. addresses.

In addition to the nominee inquiries, the company is responsible for information from two other sources. First, the company must review any reports of beneficial ownership that shareholders have filed publicly or provided to the company directly. This inquiry is not limited to the three jurisdictions mentioned above. For a widely traded company this could be a broad inquiry, although many jurisdictions do not require beneficial ownership reports or do not make the reports available to the public. The second source of information is any actual knowledge the company has about the residency of its shareholders. For example, if a company knows that one of its major shareholders is controlled by a U.S. resident, even though the shareholder itself is a Cayman Islands trust, the company may not ignore that knowledge.

How should a company apply the business contacts test?

For companies that have a majority of voting shares held by U.S. residents, the business contacts test will be the determining factor in their status as a foreign private issuer. This test has three parts.

The Location of Management. This part of the test looks at whether a majority of the company's

18. See Release No. 33-7745 (Sept. 28, 1999) [64 FR 53900].

19. In Thouret v. Hudner, 1996 U.S. Dist. LEXIS 981 Fed. Sec. Law Rp. (CCH) 99037 (S.D.N.Y. 1996) the court specifically rejected reading a beneficial ownership requirement into the foreign private issuer definition, noting that the SEC was fully aware of beneficial ownership and had made no mention of it in the foreign private issuer rules.

20. Companies seeking to rely on the SEC's exemptions for cross-border rights offers (Rule 801), cross-border exchange offers or business combinations (Rule 802), or cross-border tender offers (Tier I and Tier II) must apply these same "look through" procedures to determine the number of U.S. shareholders to whom the offer would be directed. See Cross-Border Tender and Exchange Offers, Business Combinations and Rights Offerings, Securities Act Release No. 7759 (Oct. 22, 1999) [64 FR 61382].

21. If the primary trading market is a regional one, such as EAS-DAQ, the inquiries should be directed to the clearance and settlement system associated with that market.

22. A related issue is the treatment of corporate shareholders. The staff's informal advice is that if the record owner of a company's securities is a publicly held enterprise, the company is not expected to inquire into the proportion of the enterprise's share holders that reside in the United States. It may treat the enterprise as one shareholder and its jurisdiction of organization or incorporation as its "residence." If the enterprise is private or closely held, however, the company should look through the enterprise and inquire into the residency of its owners.

executive officers or a majority of its directors are citizens or residents of the United States.[23] This calculation is done separately for each group; the executive officers and directors should not be treated as a single group for purposes of calculating the majority. The term "executive officers" refers to members of senior management with major management responsibilities or significant policy-making functions.[24] The term is not common in some countries, however, and in those cases companies should identify a group that corresponds most closely to the concept of executive officers.[25] In any event, the company should have a reasonable and objective basis for deciding which employees are considered to be executive officers, and the parameters of the group should not be changed in order to achieve a desired result.

If a company has more than one board of directors, it should determine which body performs functions most like those of a U.S.-style board of directors. If these functions are divided between both boards, that might be a basis for aggregating the members of both boards for purposes of calculating the majority. A company with dual boards of directors must apply this same functional analysis when it decides which directors should sign the company's Securities Act registration statements. It would be difficult for a company to justify making one determination for purposes of Securities Act liability and a different determination for the foreign private issuer definition.

Despite these cautions, it is clear that a company has greater flexibility to determine the outcome of this part of the business contacts test, because it has greater control over the residency of its executive officers and directors. There is no intent requirement in the test, and as long as individuals are not temporarily reassigned just long enough to influence the outcome of the test, the residency decisions are not likely to be second-guessed by the SEC staff. Companies should be careful not to ignore the citizenship part of the test, however. Even long-time U.S. expatriates may have retained their U.S. citizenship or have established dual citizenship, and they would be counted as U.S. citizens, despite their residency, for this test.

The Location of Company Assets. This part of the definition focuses on the geographic location of the company's assets.[26] The SEC staff frequently is asked for guidance in applying this test, but has declined to respond, other than to suggest informally that an accounting approach may be an appropriate place to begin. This would suggest an approach based on an analysis of the company's balance sheet and the major categories of assets presented there. Some company executives may question whether the physical location of a company's assets, as opposed to the sources of its revenues, provides the most meaningful information about the location of the company's business. Because the wording of the test is so unambiguous, however, companies should perform a balance sheet analysis.

The geographic location should be relatively easy to determine for tangible assets such as property, plant and equipment. The balance sheet analysis is more subjective, however, when it comes to other types of assets, such as goodwill or other intangibles. Most bodies of accounting principles require some sort of segment reporting of assets, and a good starting point for fixing the location of assets is to look to the segment information footnote in the company's financial statements.[27] For example, International Accounting Standard No. 14 requires disclosure of the carrying value of assets by location of the assets. Under U.S. GAAP, reporting of segments is based on a company's internal structure, but if the segments are not broken down geographically, the company must, at a minimum, report the amounts of long-lived assets located in the issuer's country of domicile and in all other foreign countries.[28] The segment disclosure is only a starting point, but a company should be prepared to explain its reasoning if it assigns one location to a category of assets for segment reporting purposes and another for the foreign private issuer definition.

The best course for most companies is to develop a standard methodology for analyzing their balance sheets, including how various categories of assets will be treated. There are no "right" answers that apply to all companies. Different categories of

23. See note 17, infra, for a discussion of issues relating to the determination of residency.

24. See Securities Act Rule 405 and Exchange Act Rule 3b-7.

25. Item 6 of the recent revisions to Form 20-F uses the expression "members of the company's administrative, supervisory or management bodies" to refer to the individuals (in addition to directors) for whom compensation information must be provided. Depending on their functions, members of this group may or may not be analogous to the company's "executive officers."

26. The definition asks whether a majority of the company's assets are located in the United States; presumably the "majority" is determined on the basis of the carrying value of the assets on the company's books, rather than using a different valuation method or the actual number of assets.

27. Other sources of information the company should review for consistency are found in its responses to Form 20-F. For example, Item 4.D. requires that companies give the location of their material tangible fixed assets, and Item 4.B. requires an overview of the business presented on the same basis as the business segments used in the primary financial statements.

28. See Financial Accounting Standard No. 131. The required disclosure for long-lived assets does not include financial instruments and certain other exceptions. If assets in an individual foreign country are material, however, they must be disclosed separately.

assets will raise different issues, and resolving those issues will depend in part on the company's business. For example:

- *Cash and cash equivalents* — In some companies all treasury operations are centralized, but in others, cash and cash equivalents may be kept in accounts in the countries where they are used to fund operations. On the other hand, the location of the account may reflect an internal investment policy and bear no relation to the location of the operations funded by the account.

- *Trade receivables* — Possible starting points might be the location of the business unit making the sale or the location of the debtor.

- *Inventories* — These might be assigned to the location of the production or distribution facility.

- *Equity investees* — Investments in other business enterprises might be located at the domicile of the investee enterprise, although a different location may be appropriate if the investee's domicile bears little or no relationship to its business operations.

- *Purchased goodwill* — A logical location is the domicile of the acquired business, unless that domicile bears little or no relationship to its business operations.[29]

- *Patents or trademarks* — A logical location might be the country where these intangibles are used, whether in ongoing research or in production of finished products.

A related issue is which GAAP should be used to measure the amount of assets after their location has been determined. The SEC staff has provided no guidance on whether a company should use the GAAP the company uses to prepare its primary financial statements or U.S. GAAP in this measurement.

The ultimate goal of the analysis is to determine whether a majority of the assets are located inside or outside the United States, not to find a precise location for every asset. The methodology the company uses should be documented, and the company's outside auditors should be given an opportunity to comment. The SEC staff is unlikely to object to a particular allocation methodology as long as it is rationally based and rigorously applied, without considering in advance what the likely result will be.

Administration of the Company's Business. The final part of the business contacts test asks whether the company's business is administered principally in the United States. The SEC staff has never defined what this means, but presumably it refers to the location where operational and policy decisions are made. This part of the business contacts test might pose a problem if, for example, a majority of the company's executive officers, directors and assets are outside the United States, but one or more key decision-makers are located in the United States and administer the business from that location.

In a 1992 no-action letter from the SEC staff to a Bahamian corporation, the corporation argued for relief from certain provisions of the proxy rules on the basis that it was not a foreign private issuer and therefore was not subject to those rules.[30] More than 50 percent of the corporation's voting securities were held by U.S. residents, so the corporation's arguments focused on the business contacts test. Factors cited to demonstrate that its business was administered principally outside the United States included the number of days the Chief Executive Officer and President each spent at the corporation's non-U.S. offices, the location where its Board of Directors and shareholders meetings were held, and the locations where each of its principal business functions were administered. The SEC staff declined to make a legal determination on the corporation's foreign private issuer status, but noted that there appeared to be some basis for its arguments and granted the requested relief.

How often should a company check its "foreign private issuer" status?

Guidance on how often a company should check its "foreign private issuer" status is available in a letter the SEC staff issued in 1993. The inquiry was made on behalf of several foreign companies that were concerned about losing their foreign private issuer status.[31] In its response, the SEC staff indicated that it was sufficient for a company to assess its foreign private issuer status on the last day of each of its fiscal quarters and upon completion of the following events:

29. The SEC staff likely would view the location of the acquired business as being the logical location of the purchased goodwill even if the reporting entity does not use "push down" accounting.

30. See staff no-action letter to Commodore International Limited (avail. October 2, 1992).

31. See staff no-action letter to Reed, Elliott, Creech & Roth (avail. March 30, 1993).

- Any purchase or sale by the issuer of its equity securities (other than in connection with an employee benefit plan or compensation arrangement, a conversion of outstanding convertible securities, or an exercise of outstanding options, warrants or rights);

- any purchase or sale of assets by the issuer other than in the ordinary course of business; and

- any purchase of equity securities of the issuer in a public tender or exchange offer by a person unaffiliated with the issuer.

The SEC staff's letter cautioned that this advice applied only to determinations of a company's foreign private issuer status for purposes of Exchange Act Rule 3a12-3(b), and expressed no opinion on whether the advice would apply to other situations in which the term "foreign private issuer" is used. Rule 3a12-3(b) provides relief from the beneficial ownership reporting and short-swing trading provisions of Section 16 and the proxy statement requirements of Section 14.

Despite the letter's cautionary language, however, the SEC staff's current informal guidance is that the frequency with which companies should check their foreign private issuer status depends on how close they are to losing that status. If a company is comfortable that it easily satisfies the definitional tests, annual assessments may be sufficient. If a company believes that its status is in question, it may need to conduct more frequent – for example, quarterly – monitoring. Certainly if the company is planning to file an SEC form that is limited to use by foreign private issuers, it should be comfortable with its representation that it meets the eligibility criteria. Other corporate events besides those listed in the SEC staff's letter also may put the company on notice that it would be advisable to check its status. Examples include a significant shift in the trading volume of company shares to the U.S. market or the sale of shares by a major shareholder.

Will the SEC challenge a company's analysis of its "foreign private issuer" status?

The SEC staff generally does not make its own analysis or question the company's analysis of its foreign private issuer status unless something comes to its attention suggesting the company has not applied the definition correctly. For example, if the company files one of the SEC forms reserved for foreign private issuers and information in the filing raises an obvious question about its foreign private issuer status, the staff may issue a comment. These forms generally contain an express representation that the registrant is eligible to file the form, so by signing the form the registrant has represented, among other things, that it is a foreign private issuer. In responding to staff comments, the company should be able to explain the methodology it followed in determining its status.

What if the company's status changes after it files a form designated for foreign private issuers?

The company generally must determine its eligibility to use an SEC form restricted to use by foreign private issuers at the time it files the form. If its status changes after filing, the company does not have to withdraw its previous filing and refile on a different form. Any pre-effective or post-effective amendments to the filing must be on the correct form, however, since each signed amendment is a fresh representation of the company's foreign private issuer status. If the company files a Form F-3 registration statement for a "shelf" offering and later ceases to be a foreign private issuer, it may continue to make "take downs" from the shelf that only require filing a prospectus supplement. Under the SEC's rules, if the SEC declares a registration statement effective without having objected to the particular form on which it was filed, that filing is deemed to be on the right form, even if it later turns out that the registrant did not meet the eligibility requirements.[32] This means that if a company's registration statement is declared effective and the company later realizes it was not a foreign private issuer at the time of effectiveness, the SEC is unlikely to challenge the company's use of the form if the staff did not raise objections prior to effectiveness.

What if the company's status changes after the end of a reporting period?

If a company satisfies the foreign private issuer definition at the end of a reporting period, but its status changes soon after, it may rely on its period-end status in determining which report form to file. For example, if a foreign company using a calendar year fiscal year satisfies the foreign private issuer definition at December 31, it may file its annual report on Form 20-F, even if it ceases to be a foreign private issuer before the Form 20-F is due. If the same com-

32. See Securities Act Rule 401(g). The only exception is for certain registration statements and post-effective amendments that become effective immediately upon filing. The SEC still might take action, however, if a company knowingly filed on the wrong form.

pany falls to satisfy the foreign private issuer definition at March 31, however, it will have to file a quarterly report on Form 10-Q within 45 days after the end of that fiscal quarter. This may result in some confusion if the company files a Form 10-Q quarterly report in mid-May, followed by a Form 20-F annual report in June. To reduce market confusion, the company may find it advisable to issue a press release or include a statement in the filing itself to explain the reason for the change in report forms.

The SEC staff has expressed concern informally with companies frequently changing back and forth from "domestic" to "foreign private issuer" reporting. If a company files a constantly changing mix of domestic and foreign periodic reports, it may cause marketplace confusion about when company information will be available.[33] The situation may arise when a company "hovers" for a period of time on the edge of satisfying or not satisfying the foreign private issuer definition. For example, a company's foreign private issuer status may depend on fluctuations in its trading volume between the U.S. and foreign markets, which can change daily. Companies in this situation should look beyond the short-term fluctuations and determine whether the changes in their status are temporary or signal a long-term shift away from foreign private issuer status.

The Importance of Advance Planning.

As described above, the consequences of losing foreign private issuer status are immediate. If a company believes its foreign private issuer status might be lost in the future, it should have a plan of action prepared so it can react immediately if it no longer satisfies the definition. Some examples of preparation that may be useful include:

- Identifying in advance the officers, directors and large beneficial shareholders who will be required to submit an initial report of beneficial ownership under Section 16.
- Giving these insiders advance warning that their sales and purchases of securities may subject them to "short-swing" trading liability and explaining the trading restrictions that Section 16 will impose.
- Having internal systems in place for the company to convert to a U.S. dollar reporting currency and to prepare condensed, consolidated financial statements for quarterly reports using U.S. GAAP.
- Making sure subsidiaries and divisions are prepared to provide U.S. GAAP financial information for the consolidated accounts.
- Designating the individuals who are authorized to speak on behalf of the company and developing policies governing corporate communications with shareholders and market professionals.[34]
- Coordinating with the company's ADR depositary and stock market personnel to determine whether the change in status will have any impact on share trading in the United States.

Other actions may be appropriate depending on the company's circumstances and the timing of its determination that it no longer is a foreign private issuer. Any preparations the company can make in advance, however, will make the transition smoother.

33. Although foreign private issuers are permitted to use the domestic forms for periodic reports, the staff informally discourages them from filing selected domestic forms in addition to their foreign private issuer reports.

34. This will position the company to comply immediately with Regulation FD. See fn. 9, infra.