



CAPITAL MARKETS ADVISORY

Time for a New Look at the U.S. Capital Markets

How the SEC's new proposed amendments would make it easier for foreign issuers to withdraw securities from U.S. markets and avoid disclosure rules.

The United States Securities and Exchange Commission (the "SEC") voted on December 13, 2006 to propose new amendments to the rules that govern when a foreign private issuer may terminate the registration of a class of equity securities and the corresponding duty to file reports, as well as when it may cease its reporting obligations regarding a class of debt or equity securities, all as required under the United States Securities and Exchange Act of 1934, as amended (the "Exchange Act," which governs the registration of classes of securities).

Just over a year ago, on December 14, 2005, the SEC originally proposed amendments in this regard. Among other matters, the original amendments used "record" ownership of U.S. residents as the operative standard for deregistration; the new proposed amendments would instead use a measure of U.S. daily trading volume as the operative standard for deregistration.

GENERAL

In connection with its vote, the SEC announced that it had reconsidered the current regime of U.S. securities law, and its formerly proposed amendments thereto, as it directly impacts foreign private issuers. Currently, delisting from a U.S. stock exchange is a relatively straightforward process, whereas the related deregistering with the SEC is considerably more difficult, if not, under certain circumstances, impossible. Such deregistration is required in order to avoid ongoing SEC disclosure and reporting obligations.

In addition, the far-reaching impact of the Sarbanes-Oxley Act of 2002, which expanded disclosure obligations to include a wide variety of corporate governance matters, created an even greater incentive for foreign private issuers to exit Exchange Act registration.

CURRENT REPORTING OBLIGATIONS UNDER EXCHANGE ACT

Generally, under the current rules, a foreign private issuer may terminate its Exchange Act registration and the reporting requirements of Section 13(a) thereof (which requires the filing of annual, periodic and other reports during the course of such registration) only if the class of the issuer's securities has fewer than 300 record holders who are U.S. residents.

Exiting the reporting requirements of Section 15(d) of the Exchange Act (which requirements are very similar to those under Section 13(a)), however, has proven practically impossible for foreign private issuers. Section 15(d) provides that the periodic reporting requirements of Section 13(a) are applicable to any foreign private issuer that files a registration statement that becomes effective under the United States Securities Act of 1933, as amended (the "Securities Act," which governs offerings of securities). Although Exchange Act Rule 12h-3 grants an automatic suspension from these Section 15(d) requirements for any foreign private issuer that has filed a Form 15 that certifies, pursuant to Rule 12h-3(b)(1)(i), that it has a class of securities held of record by less than 300 persons who are U.S. residents, subsection (c) of Rule 12h-3 makes that suspension inapplicable to any fiscal year in which a registration statement under the Securities

Act became effective.

Accordingly, although a foreign private issuer meets the 300-person deregistration requirement, Rule 12h-3(c) precludes that issuer from utilizing Rule 12h-3(b)(1)(i) to suspend its reporting requirements under Section 15(d). At best, a foreign private issuer who has done so may only suspend, and may never terminate, its duty to report arising under Section 15(d) of the Exchange Act.

NEW PROPOSAL TO ALLOW FOREIGN PRIVATE ISSUERS TO EXIT EXCHANGE ACT REPORTING SYSTEM

New Proposed Exchange Act Rule 12h-6

- New proposed Rule 12h-6 would, for the first time, allow a foreign private issuer to terminate its registration of a class of equity securities under both Exchange Act Section 12(g), and its resulting Section 13(a) reporting obligations and Section 15(d).
- New proposed Rule 12h-6 would also permit simplified deregistration of securities of foreign private issuers based on U.S. investor interest in, rather than record ownership of, those securities. This new proposed Rule would create a qualitative benchmark for measuring that U.S. investor interest in the class of securities. New proposed Rule 12h-6, instead of measuring the number of record holders of a class of securities who are also U.S. residents, uses a trading volume benchmark designed to focus on and measure relative U.S. market interest for such class of securities. This would eliminate the currently-required “head count” of U.S. resident record holders.
- The new proposed benchmark would require the comparison of the average daily trading volume of an issuer’s class of securities in the U.S. with that in its primary trading market. If the U.S. average daily trading volume of the class of securities has been no greater than 5% of the average daily trading volume of that same class of securities in the issuer’s primary trading market during a recent 12-month period, then deregistration of the securities would be permitted.
- In order to deregister, new proposed Rule 12h-6 would require that foreign private issuers either:
 - delist from the applicable U.S. stock exchange prior to deregistering, in order to meet the trading volume benchmark as of the date of delisting; or
 - wait 12 months before proceeding with deregistration in reliance on the trading volume benchmark.
- In addition, any foreign private issuer that terminates an American Depositary Receipts facility must also wait 12 months before proceeding with deregistration in reliance on the trading volume benchmark.

Additional Conditions for Equity Securities

In addition to the requirements set forth above, new proposed Rule 12h-6 would require the following of foreign private issuers of registered equity securities:

- The issuer must have been an Exchange Act reporting company for at least one year and have filed all required reports, including at least one annual report.
- The issuer must not have sold equity securities in a registered offering in the U.S. during the preceding 12 months.

The issuer must have maintained a listing for at least one year in a foreign jurisdiction that, at least in part, constitutes the primary trading market for the subject class of equity

securities.

New Proposed Exchange Act Rule 12g3-2(b)

New proposed Rule 12g3-2b would permit a foreign private issuer to claim the exemption provided by it, as follows:

Immediately upon termination of its Exchange Act reporting requirements under Rule 12h-6, so long as the issuer publishes its home country materials required by Rule 12g3-2(b) in English on its website, or by another electronic information delivery system generally available to the public in the primary trading market.

Or in the case of a non-reporting issuer, upon application to the SEC, so long as it publishes its home country materials required by Rule 12g3-2(b) in English on its website, or by another electronic information delivery system generally available to the public in the primary trading market.

Comments on new proposed Rules 12h-6 and 12g3-2(b) must be received by the SEC within 30 days of its publication in the U.S. Federal Register. We are available to provide further information and answer any questions that you may have.

This Advisory is for informational purposes only and is not intended as legal advice. For more information on the recent deregistration proposal reform or Hughes Hubbard's Capital Markets practice, please contact any of the following attorneys:

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