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POSITIONING A FOREIGN COMPANY TO BUY IN THE U.S.

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As more and more public European companies announce that they will be preparing their accounts in accordance with US generally accepted accounting principles (GAAP), or announce that they are seeking, or expect to seek, a listing in the US, the obvious question is: why? Why would a company with a listing in Europe opt to list securities, without conducting a public offering, in the US, or announce that it intends to publish US GAAP accounts? The answer may have little to do with the perceived market benefits of having securities traded in the US, and everything to do with the boom in cross-border acquisitions involving targets that are listed on a US stock exchange or quoted on Nasdaq.

The US capital markets continue to attract non-US companies. In October, the Bank of New York reported that, during the first nine months of 2000, total dollar trading volume in American Depositary Shares (ADS), the principal means by which US investors invest in non-US companies on US stock exchanges, had reached $l trillion for the first time. ADS share volume had reached 20 billion during the same period. The same report notes that 543 non-US companies have ADS programmes listed on US stock exchanges, up from 176 in 1990, and that over 1,800 non-US companies from 78 countries maintain ADS programmes in the US (the difference between the listed programmes and the total number representing over-the-counter ADS programmes). Cross-border business combinations are one of the principal drivers of this growth.

The US Regulatory Regime

The regulatory system in the US governing the offer and sale of securities is perhaps unique in its scope. All issuers are obliged to register any offers and sales of securities made in the US, regardless of whether or not the issuer is a US-listed company, and regardless of whether an issuer already has conducted a public offering in the US, unless an exemption is available. The registration requirement applies equally to offers and sales of securities for cash and exchange offers made to shareholders of a target company as part of an acquisition using stock consideration. The regulation of tender offers (for cash or stock) is subject to a separate regulatory regime. Neither regulatory regime preempts the other.

In the context of a stock-for-stock acquisition, where the target is a US company, the issuance of the securities, whether as part of a merger, or as a stock tender offer, must be registered with the Securities and Exchange Commission (SEC), unless the shareholder base of the target is sufficiently small as to allow the offer and sale to qualify for an exemption from registration. Generally, the exemption route will not be available if the target is a US public company. Companies organized in states such as California and Oregon, which have fairness hearing procedures, may qualify for an exemption. Where the US target is held by a few shareholders, the private placement route may well be available; however, given the relatively common use of stock options and other stock-based compensation schemes for employees, even by private companies, the private placement route may not be available where the relatively small base of equity holders of a private company coexists with a more broadly based pool of employee optionees.

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Where the target is a non-US company, as a result of exemptions that became effective in January 2000, a tender offer for cash or stock, or an exchange offer, may be made to US shareholders without triggering the US procedural or substantive rules applicable to tender offers, or the registration requirements applicable to the stock issued to target shareholders. These exemptions are available where the securities beneficially owned by US residents do not exceed 10% of the total of the subject class of securities. The 10% test is subject to "look-through" rules which govern how an enquiry is to be made of nominees of record, and rule on how the 10% threshold is to be calculated. Transactions that benefit from one of these exemptions can be made in accordance with local rules.

The Alternatives

For the non-US company that wants to use its stock to buy a US-listed company, or a non-US company with a significant proportion of US shareholders (so that the 10% exemption is unavailable or the traditional approach of simply excluding the US shareholders is not possible), the need to register with the SEC must be considered. The issue is then: when should the company register and how?

The non-US company seeking its entry ticket from the SEC has various options. It can:

- choose to list a class of its securities (or ADS representing such shares) on a US stock exchange;
- conduct a public offering in the US of securities (or ADS representing such securities);
- wait for the acquisition opportunity to present itself and register the stock consideration at that time; or
- offer securities under Rule 144A and agree to conduct a registered exchange offer to provide the holders with freely tradeable securities.

In each case, the company will become an SEC reporting company, and in the process will go through the SEC review process (including a review of its US GAAP financial statements or reconciliations to US GAAP). These options should not be confused with the so-called "level I" ADS programme, where a non-US company establishes an over-the-counter ADS programme and applies for an exemption from the public company reporting requirements. This Rule 12g3-2(b) information-supplying exemption is available to non-US companies which are not conducting a public offering or listing securities on a stock exchange or Nasdaq (and at the time of the application have fewer than 300 beneficial holders of their shares resident in the US).

A Listing

To list securities (or ADS) on a US stock exchange or Nasdaq, the non-US company would prepare and submit to the SEC a registration statement on Form 20-F. This statement registers the class of securities to be listed under the US Securities Exchange Act of 1934, a

prerequisite to such a listing. Although the company must also meet the eligibility criteria of the relevant exchange, file a listing application with the exchange and agree to be bound by certain qualitative listing standards, the bulk of the time and effort involved in the listing process will be focused on the SEC registration process, including the preparation of US GAAP financial statements or reconciliations to US GAAP, and the management's discussion and analysis of financial condition and results of operations.

Once the process is complete (when the SEC declares the registration statement effective), the company becomes an SEC reporting company, obliged to file annual reports with the SEC and to submit, under cover of Form 6-K, information required to be filed by the company in the local jurisdiction, or by the local exchange on which the company's securities are listed. For a company not otherwise accessing the US public capital markets or making a public acquisition, once listed, the SEC only imposes an annual filing requirement, including annual financial statements in, or reconciled to, US GAAP. The stock exchanges require the circulation of interim financial information at least on a semi-annual basis, but these can be in local GAAP.

This is not to say, however, that the non-US company need not prepare interim US GAAP financial information. The financial statement rules applicable to registration statements for listings, public offerings or acquisitions, can require inclusion of interim financial information if the registration statement is declared effective more than nine months after the company's fiscal year end. The company may also be precluded by these rules from proceeding with a listing, public offering or public acquisition during its second fiscal quarter if the financial statements (again in US GAAP or reconciled to US GAAP) for its most recent fiscal year are not yet available.

A Public Offering

A non-US company coming to the US market for the first time can choose to raise capital instead of simply establishing a US listing. The public offering requires the preparation and submission to the SEC of a registration statement on Form F-1, this time under the US Securities Act of 1933. This registration statement contains much of the information required for a listing, plus information relating to the offering. It will also contain the summary box upfront, and information with more of a marketing spin consistent with the marketing of the offering by the underwriters. It will contain risk factors, which until recently were not required in Form 20-F filings. Once this registration statement is declared effective, the company becomes subject to the same requirements as a non-US company that simply lists in the US.

A Public Acquisition

A non-US company seeking to acquire with stock, a US public company or a non-US public company with a significant US shareholder base, will prepare and submit to the SEC a registration statement on Form F-4 to register the offer to the target shareholders. This will be required for tender offers as well as for mergers. In the case of a merger involving a US public company target, the Form F-4 will also constitute the proxy statement for the target's shareholder vote. The F-4 may also be required for share exchanges involved in certain restructurings. Once the Form F-4 registration statement is declared effective, the company, if it is not already so, becomes subject to the same requirements as a non-US company that simply lists in the US.

A Registered Exchange Offer

It is not unusual for non-US companies to make their initial foray into the US capital markets on a non-registered basis, such as under Rule 144A. This eliminates the need for SEC review and gives the issuer flexibility over what information is provided to investors, though market practice may dictate that the information will be substantially similar to that provided in an SEC-registered offering. To provide investors with the benefits of registration (that is, freely tradeable securities), the company may provide investors with exchange rights, under which the company is obliged to file an exchange offer registration statement with the SEC following the closing of the Rule 144A offering. Once this registration statement is declared effective, the company again becomes subject to the same requirements as a non-US company that simply lists in the US.

Having No SEC Registration

The non-US company that has done none of this, when faced with an acquisition opportunity, faces various challenges. As speed is important in a public acquisition, having the entire SEC registration process ahead for the first time injects a substantial amount of uncertainty as to the timing of a possible closing. Particularly where the company has not begun work on the US GAAP financial statements or reconciliations, the lack of SEC registration could add several months to the process. This may not be appealing to the target's board of directors. The delay gives other companies (US or non-US) with US reporting obligations the chance to come in with a competitive stock bid that can close in as little as 30 days. If the potential for delay is insurmountable, the non-US company may be relegated to submitting a cash bid, leaving the other companies the opportunity to come in with competitive stock bid (perhaps valued at less) that offers target shareholders a tax-free alternative.

Where the target is a non-US company, the bidder with no SEC registration will have no choice but to exclude US shareholders from the offer, unless it can avail itself of the 10% exemption.

The Advantages of Prior Registration

The non-US company that has already registered, has various advantages. First, it has the requisite annual US GAAP financial information, the systems in place and the experience to prepare any interim US GAAP statements that may be required, based on the timing of the offering. (Some non-US companies prepare interim US GAAP numbers as well.) If the company has been an SEC reporting company for over one year, it is likely that it will be able to incorporate in the registration statement much of the required disclosure about itself and its business from its previously filed SEC reports. This significantly reduces the potential scope of SEC review (particularly in times when the SEC staff is overwhelmed with filings) and the likelihood that the SEC will find problems with the disclosure. In any event, existing reporting company status significantly reduces the likelihood that the SEC will have issues with the company's financial statements, since it will have already reviewed them or statements for previous years.

The non-US company that lists has advantages over and above those that arise in the public acquisition context. It can benefit from a registration regime for stock-based compensation schemes, that provides greater flexibility in crafting broad-based plans for US employees. Companies may also choose to list for market reasons or industry-specific reasons. Companies with securities listed in the US enjoy the benefits of research coverage, and the liquidity provided by the US markets. A US listing can support commitment to a US product market (particularly in the high-tech sectors) and bring companies closer to US strategic partners.

The Trend

As the pace of growth through cross-border acquisitions continues to increase, one can expect the trend among major European companies to pursue early SEC registration to continue. It may also spread to Asia as Asian companies look to the US market for acquisition opportunities or capital. Clearly, the dual-listed company has advantages in an endeavour that prizes speed and certainty. At the same time, the dual-listed company may also reap other benefits of having securities traded in the US markets, and of having embraced the more detailed disclosure practices mandated by the SEC.

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